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TRANSCRIPT OF RECORD.

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1898.

No. ~~12~~ 22.

**THE LACKAWANNA IRON AND COAL COMPANY ET AL.
PETITIONERS,**

vs.

THE FARMERS' LOAN AND TRUST COMPANY ET AL.

**ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT
OF APPEALS FOR THE FIFTH CIRCUIT.**

**PETITION FOR CERTIORARI FILED SEPTEMBER 4, 1898.
CERTIORARI AND RETURN FILED MARCH 19, 1899.**

3
(16,864.)

(16,664.)

SUPREME COURT OF THE UNITED STATES.

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No. 162.

THE LACKAWANNA IRON AND COAL COMPANY ET AL.,
PETITIONERS,

vs.

THE FARMERS' LOAN AND TRUST COMPANY ET AL.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT
OF APPEALS FOR THE FIFTH CIRCUIT.

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a UNITED STATES OF AMERICA, }
 Fifth Judicial Circuit. }

Pleas and proceedings had and done at a regular term of the United States circuit court of appeals for the fifth circuit, begun on the 3d day of November, A. D. 1896, and held in the court-room of said court, in the city of New Orleans.

Proceedings before the Honorable Harry T. Toulmin, United States district judge for the southern district of Alabama, the Honorable T. S. Maxey, United States district judge for the western district of Texas, and the Honorable Charles Parlange, United States district judge for the eastern district of Louisiana.

THE LACKAWANNA IRON & COAL COMPANY ET AL. }
 vs. }
 "THE FARMERS' LOAN & TRUST COMPANY ET AL. }

Be it remembered, that heretofore, to wit, on the 4th day of May, 1896, a transcript of the record of the above-stated cause from the circuit court of the United States for the eastern district of Texas, was filed in the office of the clerk of the said United States circuit court of appeals, a true copy of which is set out in the pages hereto annexed.

1-7 In the Circuit Court of the United States for the Eastern District of Texas, in the Fifth Circuit, Holding Sessions at Galveston.

THE FARMERS' LOAN AND TRUST COMPANY, Trustee, }
 vs. } No. 227.
 THE HOUSTON & TEXAS CENTRAL RAILWAY COMPANY, } Equity.
 Charles Dillingham, Receiver, and George E. Downs. }

Be it remembered that in the above entitled and numbered cause, lately pending in said court, in which final decrees were rendered at the regular February term of said court, 1896, to wit: on the 26th day of February, A. D. 1896, in interventions of the Lackawanna Iron and Coal Company, the Southern Development Company, the Morgan's Louisiana and Texas Railroad and Steamship Company, the Pacific Improvement Company, Collis P. Huntington and E. H. R. Green and George E. Downs, the Honorable David E. Bryant, judge of the district court of the United States for the eastern district of Texas, presiding, the following proceedings were had and taken in said court, to wit:

8 Circuit Court of the United States, Eastern District of Texas.

THE FARMERS' LOAN AND TRUST COMPANY, Complainant,	} No. 227. Equity.
vs.	
THE HOUSTON AND TEXAS CENTRAL RAILWAY COMPANY et al., Defendants.	

Original Bill of Complaint.

(Waco and Northwestern Division first mortgage.)

Turner, McClure & Rolston, complainant's solicitors, 20 Nassau street, New York.

Filed of date April 6th, 1889. Don A. Pardee.

Filed April 6th, 1889. C. Dart, clerk.

To the judges of the circuit court of the United States for the eastern district of Texas, sitting in equity :

The Farmers' Loan and Trust Company, a corporation duly created under the laws of the State of New York, a citizen of said State, having its principal office and place of abode in the city of New York, brings this its bill of complaint against the Houston and Texas Central Railway Company, a corporation created under the laws of the State of Texas, a citizen of said State, having its principal office and place of abode in the city of Houston, in said State, and against Charles Dillingham, as receiver of the Houston and Texas Central Railway Company, a citizen of the State of Texas, having his place of abode in the city of Houston, in said State.

And thereupon your orator complains and alleges :

I. Your orator is a corporation duly organized and existing
9 under the laws of the State of New York, and is fully authorized and empowered to receive and hold in trust the lands, railroads, franchises and other property conveyed to it in trust as hereinafter fully stated, and to execute the trusts reposed in it under and by virtue of the mortgage or deed of trust hereinafter set forth. The property which is the subject-matter of this suit, being the property affected by the mortgage to your orator hereinafter set forth, is now in the actual custody of this honorable court through its receiver, duly appointed, as hereinafter more fully stated.

II. The defendant, The Houston and Texas Central Railway Company, is a corporation duly organized and existing under the laws of the State of Texas, having been first known as the Galveston and Red River Railway Company, and its name having been changed by an act of the legislature of the State of Texas, approved September 1, 1856, to the Houston and Texas Central Railway Company. It was by said act invested with the right of making, owning and maintaining a railroad from Galveston bay or its contiguous waters to Red river; and by another act of the legislature, approved May 24, 1873, the Waco and Northwestern Railroad Company, a duly organized corporation, with all its properties, rights, privileges and

franchises, was merged in the Houston and Texas Central Railway Company and became a part thereof. The said Houston and Texas Central Railway Company (which, for convenience, will herein be designated as the railway company), by virtue of said acts and others, and in every respect according to law, became a corporation owning and operating several lines of railroad, namely, a line from Houston to Denison, a distance of 345 miles, known as the main line, a line from the main line at Hempstead to Austin, a distance of 118½ miles, known as the Western division, and a line from the main line at Bremond to Ross, a distance of 58 miles, known as the Waco and Northwestern division, which latter division, with certain lands and other properties, constitutes the particular subject-matter respecting which this bill is filed.

III. Under certain acts of the legislature of Texas, and especially an act entitled "An act to encourage the construction of
10 railroads in Texas by donations of lands," approved January 30, 1854, and several acts supplemental thereto and amendatory thereof, the railway company became entitled to receive from the State of Texas, to aid in the construction and equipment of its railroad, sixteen sections or square miles of land of the public domain of said State, equal to 10,240 acres, for every mile of its railroad that had been built and that might be built in the future, as the same should be so built.

IV. The said railway company, prior to April 1, 1881, executed and delivered the following mortgages or deeds of trust, namely :

1. A mortgage dated July 1, 1866, covering the main line and ten sections of land for each mile thereof, commonly known as the main-line first mortgage, and under the same Nelson S. Easton and James Rintoul are substituted trustees.

2. A mortgage dated December 21, 1870, covering the Western division and ten sections of land for each mile thereof, commonly known as the Western Division first mortgage, and under the same Nelson S. Easton and James Rintoul are substituted trustees.

3. A mortgage dated June 16, 1873, covering the Waco and Northwestern division and also 6,000 acres of land for each mile thereof, commonly known as the Waco and Northwestern Division first mortgage, which mortgage was made to your orator, as trustee. Your orator still remains trustee under the same, and files this bill in that capacity.

4. A mortgage dated October 1, 1872, covering the main line and Western division as a second mortgage, and also 3,840 acres of land per mile of completed road. This mortgage is commonly known as the main-line and Western Division consolidated mortgage.

5. A mortgage dated May 1, 1875, covering the Waco and Northwestern division and also 6,000 acres of land per mile of completed road. This mortgage is commonly known as the Waco and Northwestern Division consolidated mortgage.

6. A mortgage dated May 7, 1877, covering all the property of said railway company, and commonly known as the income and indemnity mortgage.

- 11 7. A mortgage dated April 1, 1881, covering all the property of said railway company, and commonly known as the general mortgage.

V. On or about February 16, 1885, the Southern Development Company, a California corporation, instituted suit in this court against the railway company, and such proceedings were thereupon had that the railway company and all its property of every sort and description were placed by order of this court, dated February 20, 1885, in the hands of receivers thereby appointed, said receivers being the defendant, Charles Dillingham and one Benjamin G. Clarke. The persons so named as receivers, immediately on their appointment qualified as such and took possession of all the property of the railway company and entered upon the discharge of their duties as receivers, and they continued to act as such until the May, 1886, term of this court, when such proceedings were had in said cause so brought by the Southern Development Company as aforesaid that this court made a decree in said cause, entered May 27, 1886, ordering that certain demurrers filed in said cause be sustained and that the whole bill and supplemental and amended bill of the Southern Development Company, against all the defendants therein named, be and the same thereby were dismissed for want of equity, with costs. Bills in equity, however, having been filed before that time in this court by the trustees of the said main-line first mortgage, and Western Division first mortgage and general mortgage, for the foreclosure of said mortgages respectively, such proceedings were thereupon had, that such bills so filed for such foreclosure were consolidated by an order of this court, entered May 27, 1886, and Nelson S. Easton, James Rintoul and Charles Dillingham were appointed receivers of all the property of the railway company, in the room and stead of the receivers appointed in said cause of the Southern Development Company.

12 VI. In the said consolidated cause pending in this court, Nelson S. Easton and James Rintoul, trustees, and The Farmers' Loan and Trust Company, trustee, were complainants, and the said Houston and Texas Central Railway Company and others were defendants. In said cause, cross-bills were subsequently filed for the foreclosure of the main-line and Western Division consolidated mortgage, the Waco and Northwestern Division consolidated mortgage, and the income and indemnity mortgage. Thereupon a decree of foreclosure and sale was entered by this court in said cause, in all respects according to law, at the May term of this court, held at Galveston on or about May 4, 1888. In and by said decree, to which your orator prays to refer as in all respects a part hereof, this court ordered, adjudged and decreed that unless said railway company should, within thirty days, pay into court the amounts due upon its mortgages not including the Waco and Northwestern Division first mortgage, then the mortgages, with that exception, should be foreclosed and all its property should be sold, as in said decree particularly provided, the sale, however, of the property, premises and franchises covered by the said first mortgage

of the Waco and Northwestern division to your orator as aforesaid, to be made subject to said first mortgage on said property.

VII. In pursuance of said decree (the payments of the mortgage indebtedness thereby ordered not having been made) the entire property of the Houston and Texas Central Railway Company was sold by the said master commissioner, September 8, 1888. At such sale all the property of every kind and description covered by the Waco and Northwestern Division first mortgage to your orator, including lands estimated at about 277,220 acres, was sold by the said master commissioner, and purchased by ——. The purchase so made by said Downs was made subject in every respect to the lien of the Waco and Northwestern Division first mortgage on said property, so made to your orator, as aforesaid, and a deed of said property has been made and delivered to said Downs, as in said decree provided, but in said deed it is expressly stated that the same was made subject in all respects to the lien of the said first mortgage of the Waco and Northwestern division, made to your orator as aforesaid.

VIII. Nelson S. Easton and James Rintoul, who were appointed receivers with Charles Dillingham, as above stated, have been relieved, of their duties as such receivers, by an order of this court made in said consolidated cause December 7, 1888, and said

13 Charles Dillingham is now in possession as sole receiver of all the property formerly of said railway company, defendant, including the property of every sort and description covered and affected by the Waco and Northwestern Division first mortgage, made to your orator, as aforesaid. Your orator prays to refer to the various pleadings, orders and other papers filed in the causes above mentioned, as parts of this its bill of complaint.

IX. The Waco and Northwestern Division first mortgage, made to your orator by the railway company as aforesaid, was made in all respects according to law, and the same is a first-mortgage lien upon all the property therein described. Your orator annexes to this, its bill of complaint a copy of the said first mortgage, and referring thereto, prays that the same may be taken in all respects as a part thereof.

X. The said Waco and Northwestern first mortgage was made by the railway company to secure a series of its own bonds for \$1,000 each, payable to bearer on July 1, 1903, with interest thereon at seven per centum per annum, payable from July 1, 1873, semi-annually, in gold, on the first days of January and July of each year, free from all deduction of taxes, until the principal should be paid, on presentation of certain annexed coupons, at the agency of the railway company in the city of New York or in London, as the said coupons might be stamped. It was in said bonds, and each of them provided that the same should not become obligatory, unless the certificate endorsed thereon was signed by your orator, as trustee, or its successor in the trust; and your orator did so sign and certify 1,140 of the said bonds, and it is informed, and therefore alleges that of the said bonds so certified by it, 1,140 bonds representing \$1,140,000 of principal are now outstanding and un

paid, and entitled to the benefit of the security of said mortgage or deed of trust.

XI. In and by said mortgage or deed of trust the said railway company, to secure the payment of said bonds, conveyed to your orator in trust, and to its successors and assigns, all and singular the said railway company's railway, known as the Waco and Northwestern division, built and to be built, beginning at a point
14 on the main line of the Houston and Texas Central railway, in the town of Bremond, Robertson county, passing through the city of Waco, in McLennen county, to Red river, and thence to the northern boundary line of said State, together with all side tracks, turnouts, rolling stock, equipment and materials, all right of way and tracks, depot and shop grounds, tenements, hereditaments, rights and franchises, including and meaning to include all the property, real and personal, then acquired, or which might thereafter be acquired by the said company in the said State of Texas, pertaining to the operation of said division, and also all and singular six thousand acres of land per mile of completed road of the said division, said lands selected and to be selected from ten thousand two hundred and forty (10,240) acres of land per mile of completed road donated by the State of Texas, to aid in the construction of the said Waco and Northwestern Railroad Company.

XII. In the said mortgage or deed of trust, it was, among other things, provided that in case the said railway company should fail to pay the principal, or any part thereof, or any instalment of the interest, or any part thereof, or any of the said bonds, at any time when the same should become due and payable, according to the tenor thereof, and for sixty days after having been demanded, it should be competent for your orator, as trustee, its successors and assigns, to enter upon the said railway and the premises and property therein conveyed, by its attorneys and agents, and take possession of the same, without let or hindrance of the railway company, and every part and parcel thereof and the appurtenances, and appoint an agent to operate and manage the same, and receive the revenue and income thereof, applying the said fund, after the deduction of taxes, necessary expenses and counsel fees, to keep the same in good order and repair, and the surplus to pay the interest and principal of all the bonds which might be due and outstanding and secured thereby *pro rata*, and thereafter to the payment of any contribution due to the sinking fund therein established; and upon the request of the holders of one-fifth in amount of the bonds so in
15 default which might be at any time outstanding under the said deed of trust, it should be the duty of your orator, as trustee, by its president or agent duly appointed in its behalf, to enter upon and take actual possession, with or without entry or foreclosure of said railway and property therein described, and all and singular each and every part and parcel thereof, and assume its management until the arrears of both principal and interest be paid, or the property sold, as therein prescribed, receiving the rents, revenues and income thereof and applying them in the same manner as above stated.

XIII. Default has been made by the railway company and by said purchaser, Downs, and Receiver Dillingham, in the payment on the first day of January, 1886, of the coupon interest due on that day on all the said first-mortgage bonds, and all interest on the said bonds from that day remains overdue and unpaid, including said coupon interest, and each instalment of coupon interest on the same which matured subsequently. Payment of some of such interest has been demanded more than sixty days since.

XIV. By reason of the matters and things hereinbefore alleged, there is due to your orator, as trustee under the aforesaid first mortgage or deed of trust of the Waco and Northwestern division of the Houston & Texas Central Railway Company, or to the holders of said bonds, the amount of the coupon interest which fell due on each and every of said bonds on the first day of January, 1886, and also each and every instalment that has fallen due on the same since that day, with interest on each instalment of the said coupon interest from the time when the same fell due as aforesaid; and no proceedings have been had at law or in equity for the collection of the said mortgage debt or any part thereof save only this suit and certain petitions filed in the said consolidated cause of *Easton et al., vs. The Houston & Texas Central Railway Company* as aforesaid, which petitions, so far as they affected any of the interest on said bonds hereby claimed to be still due and outstanding, have been denied.

XV. Your orator was served, on or about March 5, 1889, with a certain paper-writing in the words and figures following, and subscribed as follows:

16 "To the Farmers' Loan and Trust Company, trustee under the seven per cent. mortgage of the Houston & Texas Central Railroad Company, Waco and Northwestern division:

"We, the undersigned, owners and holders of the seven per cent. first-mortgage bonds of the Houston & Texas — Railway Company, Waco and Northwestern division, to the amounts set opposite our names respectively, do hereby call upon and demand of you that you at once proceed by demand, action or otherwise, to enforce and secure our rights as such bondholders, and execute the duties incumbent upon you under the deed of trust, and thereon to take possession of and operate the mortgaged premises pursuant to the provisions of the mortgage, and thereby secure the payment of interest on such bonds; but we expressly request that until further requested by us, you do not commence or take proceedings to foreclose or enforce the payment of the principal, it being our desire that the interest, not the principal, be enforced.

"Dated, New York, December 25, 1888.

under which you are trustee. We are advised that the lands covered by that mortgage ought to be disposed of at the earliest practical moment, so as to avoid the risk of forfeiture. We do not think it wise or prudent for the trust company to take possession of or to operate a branch road such as the Waco and Northwestern division of the Houston and Texas Central railroad is. We regard such a course as prejudicial to the true interests of the bondholders, and likely to imperil both their principal and interest. We therefore request that instead of taking possession of the property you at once commence proceeding- for the foreclosure of the mortgage.

"New York, March 9, 1889.

"Bonds.

\$215,000.

Percy R. Pyne, } Trustees under last will and
Law Turnure, } testament of Moses Taylor,
M. Taylor Pyne, } deceased.

19,000.

Prescott Hall Butler, trustee under will of
Charles P. Clinch, dec'd."

XIX. The persons subscribing these various writings are, as your orator is informed and believes, holders and owners of the bonds secured by the said Waco and Northwestern first mortgage made by the railway company to your orator as aforesaid, to the extent and amount which they by said writings profess to hold and own; and since the property of the railway company has been in the hands of receivers as aforesaid, your orator has received no request of any kind or description from any holder or owner of such bonds to proceed to enforce the provisions of the said mortgage, nor any intimation or expression of any positive wish or desire on the part of such bondholders as to what the trustee should do in the premises, save only as above stated.

XX. Your orator is informed by the writings served on it as aforesaid and otherwise, that there is a difference of opinion between the holders of the bonds secured by said first mortgage of the railway company on the Waco and Northwestern division, as to the proper course to be pursued under the existing circumstances. From the said requests it seems, and your orator alleges, that holders of bonds to the extent of \$556,000 of principal, now desire your orator, as trustee, to proceed under those clauses of said mortgage which provide for your orator, as trustee, taking possession of the mortgaged premises and operating the same; that holders of bonds to the amount of \$234,000 of principal, are opposed to that course, desiring the foreclosure of said mortgage; that holders of \$300,000 of said bonds (being unknown to your orator) have expressed no opinion on the subject whatever, and that the holder of \$250,000 of said bonds, having at one time joined in the first request, has expressed her wish to withdraw therefrom.

19 In consequence of the embarrassed condition of the financial affairs of the Houston and Texas Central Railway Company, and on account of the many difficulties which are manifest upon and from all allegations hereinbefore contained involved in

the execution of your orator's said trust, it is impossible for your orator, as trustee, under the said mortgage or deed of trust, to execute its said trust in the way and manner specified and provided in and by said mortgage or deed of trust without the aid or interposition of this honorable court in chancery sitting; nor can the said trust be executed, as your orator is advised and charges, and the rights of all parties be ascertained and fully protected in the premises, otherwise than by a judicial sale of the mortgaged premises, and all the franchises, property, premises and appurtenances covered by said mortgage or deed of trust. Until such sale can be had, and the proceeds thereof distributed, your orator is likewise advised and charges that it is expedient and necessary that the franchises, property, premises and appurtenances so mortgaged to your orator in trust as aforesaid, be placed in the hands and under the control of your orator, as trustee in possession, or of a receiver, with such powers and control over the same as to the court shall seem right and equitable to be conferred.

In consideration thereof, and forasmuch as your orator is remediless in the premises by the rules of the common law, and can have adequate relief only in a court of equity, where matters of this nature are properly cognizable and relievable; to the end, therefore, that the said defendants may, if they can, show why your orator should not have the relief hereby prayed, and that they may separately and severally answer make (but not under oath, their answer under oath being hereby expressly waived), according to the best of their knowledge, information and belief, to all the matters and charges aforesaid, and that as fully in every respect as if the same were here again repeated, and they thereunto particularly interrogated; that your orator (or a receiver appointed by this court in this cause) may be placed in possession of all the rights, franchises and property, of every kind and description, covered by the
20 said mortgage or deed of trust, of the Waco and Northwestern division of the Houston and Texas Central railway, with power and authority to operate said railroad under the protection of this court, with the usual powers of receivers in such cases, and with power to proceed to recover by suit or otherwise all property in the hands of other parties covered or affected by the said mortgage or deed of trust; that all the rights, franchises and property of every sort and description described in said mortgage may be declared subject to the lien of the same, and that the same may be held and declared to be a first lien upon the same; that an account may be taken of the amounts due upon the bonds secured by the said mortgage or deed of trust, and now outstanding, for interest, being the amount of the unpaid coupons of said bonds, with interest thereon, and on each of them, from the time when the same respectively fell due; that the amount so found due and also the amount of the principal of the said bonds may be found to be the first lien upon the property covered by the said mortgage or deed of trust, according to the terms of the same; that the defendant, Houston and Texas Central Railway Company and the present owners of said property may be decreed to pay the amount so found due upon

said coupons, with interest thereon at a short day to be fixed by the court; that in default thereof all the property, franchises and premises covered by the said mortgage or deed of trust, being the Waco and Northwestern division of the Houston and Texas Central Railway Company, and all the lands and properties contained and set forth in the description in said mortgage or deed of trust, may be sold under a decree of this court, according to the law and practice of this court, to satisfy the amount so found due; that out of the proceeds of said sale or the net earnings of said property there may be paid first the costs and expenses of your orator in this suit, and all its expenses of every sort and description involved in the execution of its trust, including proper attorneys' and counsel fees, with a proper compensation to your orator for its own services as trustee, to be allowed by the court, and that the residue thereof may be applied to the payment of the amount due upon the said first-

21 mortgage bonds and the coupons thereto, with interest thereon;

that if there be any surplus, it may be applied in such way as this court may direct; and that the defendants in this suit may be barred of and from any equity of redemption of, to, and in the said property and franchises; and that any deficiency on such sale may be entered in this cause as a judgment against the Houston and Texas Central Railway Company, and that your orator may have such other and further relief in the premises as the circumstances of the case may require, and as may be agreeable to equity.

May it please your honors to grant unto your orator a writ of subpoena issuing out of and under the seal of this honorable court, directed to the defendants, The Houston and Texas Central Railway Company, and Charles Dillingham, as receiver of the Houston & Texas Central Railway Company to appear and answer this bill.

And your orator will ever pray, etc.

THE FARMERS' LOAN &
TRUST COMPANY,

By R. G. ROLSTON, *President.*

[L. s.]

TURNER, McCLURE & ROLSTON,
WILLIE, MOTT & BALLINGER,

Complainant's Solicitors.

HERBERT B. TURNER, *Of Counsel.*

STATE OF NEW YORK, }
Southern District of New York, } ss :

I, Rosewell G. Rolston, being duly sworn, depose and say, that I am the president of The Farmers' & Loan Trust Company, the plaintiff above named, and have been such president for a number of years past; that I have read the foregoing complaint and know the contents thereof, and that the same is true to my own knowledge, except as to those matters therein stated to be alleged on information and belief, and as to those matters I believe it to be true.

I further say that the reason why this verification is not made by the said plaintiff, is that it is a corporation, that I am an officer of

the same to wit: the president, and that my knowledge is derived
 22 from having taken my part in the transactions spoken of
 and otherwise, and my grounds of belief are information
 communicated to me by the agents of said corporation and
 others. I further say that the seal affixed to said complaint is the
 corporate seal of said plaintiff, and was by me affixed to the same
 by authority of said corporation.

R. G. ROLSTON.

Sworn to before me this 29th day of March, 1889.

JOHN McCLURE,
Notary Public, New York County.

Houston & Texas Central railway, Waco and Northwestern division.

*Mortgage or Deed of Trust to the Farmers' Loan and Trust Company
 of the City of New York, Trustee.*

This indenture, made the sixteenth day of June, in the year of
 our Lord one thousand eight hundred and seventy-three (A. D.
 1873), between the Houston & Texas Central Railway Company, a
 corporation under the laws of the State of Texas, of the first part,
 and the Farmers' Loan and Trust Company of the City of New
 York, a corporation existing under the laws of the State of New
 York, trustee, party of the second part.

Witnesseth: Whereas, the party of the first part, under and by
 virtue of the laws of the State of Texas, has acquired by purchase,
 the charter and the right and title of the Waco & Northwestern
 Railroad Company to, and possession of, its line of railway, and said
 line, by an act of the legislature of the State of Texas, entitled "An
 act to provide for the merger of the Waco & Northwestern Railroad
 Company, with its properties, rights, privileges and franchises, in
 the Houston & Texas Central Railway Company," approved on the
 twenty-fourth day of May, A. D. eighteen hundred and seventy-
 three, has been merged and consolidated with and made a part of
 the Houston & Texas Central Railway Company, and the said con-
 solidation has been formally accepted by the said companies.

And whereas, the said Houston & Texas Central Railway Com-
 23 pany, to meet the expense of constructing and equipping the
 line of the said Waco & Northwestern railroad, known since
 the merger or consolidation as the "Waco and Northwestern
 division," about fifty miles of which have already been constructed
 and are in actual use in the daily running of trains, have resolved
 to issue and negotiate, as by law they are duly authorized, a series
 of bonds of one thousand dollars each, at the rate of twenty thou-
 sand dollars to each mile of completed road, which said bonds and
 the interest to become due thereon, are to be all equally secured by
 these presents, although issued at different times, and to be authen-
 ticated by a certificate signed by the said trustee. The said bonds
 and coupons to be substantially in form as follows:

(Bond.)

THE UNITED STATES OF AMERICA, *State of Texas.*

The Houston & Texas Central Railway Company.

No. —.

\$1,000.

First-mortgage, Land grant, Sinking-fund, Gold-bearing Bond—Interest at 7 per Centum per Annum, Payable Semi-annually.

The Houston & Texas Central Railway Company, for value received, promise to pay to bearer the sum of one thousand dollars in United States gold coin, at its office in the city of New York, on the first day of July, A. D. one thousand nine hundred and three, with interest thereon, at the rate of seven per centum per annum, from the first day of July, A. D. one thousand eight hundred and seventy-three, payable semi-annually, in gold, on the first days in January and July of each year, free from all deduction of taxes, until the principal sum be paid, on presentation of the annexed coupons, at the agency of the said company in the city of New York, or in London, as the said coupons may be stamped.

This bond is one of a series of one thousand dollars each, numbered consecutively from one upward, issued twenty to each mile of completed road, all of which are equally secured by a deed of trust, bearing date June sixteenth, eighteen hundred and seventy-three, executed by said company unto the Farmers' Loan and Trust Company of the City of New York, trustee, conveying all and singular,

the entire line of said company's railway built and to be built, starting from the town of Bremond, in the State of Texas, and passing through the city of Waco, to the Red

river, and thence to the northern boundary line of said State, together with all the side tracks, turnouts, rolling stock and other equipment, all right of way, depot and shop grounds, tenements, hereditaments, rights and franchises and all the property, real and personal, acquired and hereafter to be acquired, pertaining and necessary to the operation of the above-described division of said railway; and also, all and singular, six thousand acres of land per mile of completed road—said lands, selected, and to be selected, from the ten thousand two hundred and forty (10,240) acres of land per mile of completed road, donated by the State of Texas to aid in the construction of the said road, now known as the Waco & Northwestern division of the Houston & Texas Central railway.

This bond is entitled to the privileges of a sinking fund, and is convertible into, or receivable at par in payment for any of the lands of the said railway company conveyed to said trustee to secure the payment of this bond by the said deed of trust.

This bond may be registered on the books of said railway company at its agency in the city of New York. After such registration, no transfer, except on the books of said company, shall be valid. On a registration of ownership the holder may, at his option, surrender the coupons, which will then be cancelled, and thereafter interest will be payable to the registered holder or his attorney.

This bond shall not become obligatory, unless the certificate endorsed hereon is signed by the said trustee or its successor in this trust, who shall countersign and deliver this series of bonds at the rate of twenty to each mile of completed road only upon the certificate of the company's chief engineer that each mile is completed.

In witness whereof, the said Houston and Texas Central Railway Company has caused its corporate seal to be hereto affixed [L. s.] and the same to be attested by the signatures of its president and secretary, the twentieth day of June, in the year of our Lord one thousand eight hundred and seventy-three.

— — —, *Secretary.*

— — —, *President.*

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\$35.

(Coupon.)

The Houston and Texas Central Railway Company will pay to bearer, on the first day of January, 1874, at its agency in the city of New York, on the surrender of this coupon, thirty-five dollars in United States gold coin, free of all taxes, for semi-annual interest on the first-mortgage bond upon its Waco and Northwestern division.

No. —.

— — —, *Secretary.*

Trustee's Certificate.

The Farmers' Loan and Trust Company of the City of New York hereby certifies that this bond is one of the series of bonds described in and secured by the mortgage or deed of trust within mentioned, and that no more such bonds have been certified by this company than are authorized by said deed of trust.

Now, therefore, this indenture further witnesseth, that for and in consideration of the premises, and of the sum of one dollar to it duly paid by the party of the second part, the receipt whereof is hereby duly acknowledged, and in order to secure the payment of the principal and interest of the said bonds, the Houston & Texas Central Railway Company doth hereby grant, bargain and sell, convey, transfer and confirm unto the said party of the second part, in trust, and to its successors and assigns, all and singular, the said company's railway, known as the Waco & Northwestern division, built and to be built, beginning at a point on the main line of the Houston & Texas Central railway, in the town of Bremond, Robertson county, passing through the city of Waco, in McLennan county, to the Red river, and thence to the northern boundary line of the said State, together with all side tracks, turnouts, rolling stock, equipment and materials, all right of way and tracks, depot and shop grounds, tenements, hereditaments, rights and franchises, including and meaning to include all the property, real and personal, now acquired, or which may hereafter be acquired, by the said company in the said State of Texas, pertaining to the operation of the said division; and also, all and singular, six thousand acres

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of land per mile of completed road of the said division—said lands selected, and to be selected, from the ten thousand two hundred and forty (10,240) acres of land per mile of completed

road, donated by the State of Texas, to aid in the construction of the said Waco & Northwestern railroad.

To have and to hold the said railway, property, lands, premises and rights hereby conveyed, or intended so to be, unto the said The Farmers' Loan and Trust Company of the City of New York, trustee, and its successors or assigns, *in trust*, for the owners and holders of said bonds, or any of them, subject to the terms and stipulations of said bonds, and the interest coupons thereto annexed, and the provisions of the charter of the said company; and also subject to the possession and management of said party of the first part, and its assigns, so long as said company shall well and truly perform, all and singular, the stipulations of the bonds aforesaid, and the covenants of this indenture.

And in case the said Houston & Texas Central Railway Company shall fail to pay the principal, or any part thereof, or any installment of the interest, or any part thereof, on any of the said bonds at any time when the same shall become due and payable according to the tenor thereof, and for sixty days after having been demanded, it shall be competent for the said trustee, its successors or assigns, to enter upon the said railway and the premises and property herein conveyed, by its attorneys and agents, and take possession of the same without let or hindrance of the said first party, and every part and parcel thereof, and the appurtenances, and appoint an agent to operate and manage the same, and receive the revenue and income thereof, applying the said fund, after deducting taxes, necessary expenses and counsel fees, to keep the same in good order and repair, and the surplus to pay the interest and principal of all the bonds which may be due and outstanding and secured hereby, *pro rata*, and thereafter to the payment of any contributions due to the sinking fund herein established. And upon the request of the holders of one-fifth in amount of the bonds so in default which may be at any time outstanding under this deed of trust, it shall be the duty of said second party, by its president or agent, duly appointed in its behalf, to enter upon and take actual possession with or without entry or foreclosure, of said railway and property herein described, and all and singular each and every part and parcel thereof, and assume its management until the arrears of both principal and interest be paid, or the property sold as herein prescribed, receiving the rents, revenues and income thereof, and applying them in the same manner as above stated.

And in case default shall be made in the principal sum or sums, by virtue of the said bonds or any of them, or any part thereof, at maturity, the said second party shall, on the written request of a majority of the holders of the bonds so in default then unpaid and outstanding, institute the proper proceedings in the proper courts to procure a decree of sale of said premises and property, and all and singular every part and parcel thereof, or so much thereof as may be necessary to make the payments so in default.

It being understood that the lands hereby conveyed, or so much thereof as may be necessary, shall be first sold by said second party at public or private sale for the best price which can be obtained for

the same without any legal proceedings whatsoever; or the second party may cause the entire railway of the said Waco and North-western division, with all its rights, appurtenances, equipments and material of every kind, to be sold at public auction to the highest bidder, first giving three months' notice thereof before the day of sale in one or more of the daily newspapers published in each of the cities of New York, Boston and Houston, stating the time, place and terms of sale with a description of the property to be sold, and upon such sale of the whole or any part of the said property being made, and receiving the purchase-money therefor, the said party of the second part shall execute a deed in fee-simple of the same, which deed shall be a bar against the party of the first part, its successors or assigns, from and against all claim of the said first party, and all its right of redemption therein, and shall convey full and absolute title therein to the purchaser, free and clear of all encumbrance thereon, and of all claims, rights or equities of the said party of the first part, its successors or assigns, and all persons claiming under them forever. And the receipt of said trustee

28 shall be a full and sufficient discharge of said purchaser thereof, and said purchaser, holder of said receipt, shall not be liable or in any way bound to see said purchase-money applied to this trust or in any way answerable for its loss or misapplication, or obliged to inquire into the authority for making such sale. And the said party of the second part shall, after deducting from the proceeds of said sale the costs, counsel fees, and all payments for taxes and assessments and expenses thereof and of managing the said property, and enough to indemnify and save itself harmless from all liabilities arising from this trust, apply so much of the proceeds of the sale of said property as may be necessary to the payment *pro rata* of all the interest and principal of said bonds outstanding as may be unpaid, and shall pay the residue thereof, if any, to the party of the first part, its successors or assigns. It being expressly understood and agreed by the said first party, that in no case shall any claim be made or advantage taken of any valuation, appraisalment or extension laws now existing or hereafter to be enacted, by the said party of the first part, its successors or assigns, the benefit of all such laws being expressly waived; nor shall any proceedings be taken to prevent such entry or sale or conveyance as aforesaid.

And it is further covenanted on the part of the said first party, its successors and assigns, that the proceeds of this series of bonds shall be applied, in good faith to the construction, improvement and equipment of said division, made and to be made, and putting the same into operation. It is, however, expressly agreed, that the said party of the first part may dispose of the current net revenues and income of all the said property and railway hereby conveyed, in such manner as it shall deem best, until default shall be made in the payment of the interest or principal of said bonds, or of any one or more of them, and shall have the right to sell and dispose of any of such real estate, or other property, as it may own or acquire, which may not be needed or required for the purposes and business

of the said Waco and Northwestern division, except in the case of the six thousand acre-per mile of completed road, and which sale and conveyance of such outside property, shall transfer the said property and title free from encumbrance of this mortgage or deed of trust, and to change its tracks, and make any and all alterations necessary for the benefit of the same. And it is further expressly agreed and understood that every bond issued under this mortgage or deed of trust shall be countersigned by the said party of the second part, and certified to be one of the series authorized to be issued by virtue hereof, or under this deed of trust, and no bond shall be valid under this deed or entitled to its protection and security unless it shall be so certified.

And the said party of the first part hereby covenants and agrees to and with the said second party that the said first party shall pay to the said trustee, on or about the first day of December, A. D. eighteen hundred and eighty, and of each succeeding year until the series of bonds provided for in this indenture shall be paid off and extinguished, a sum annually equal to two per centum of the amount of such bonds as shall then be outstanding and unpaid; which moneys, together with all moneys which may be received by said second party as such trustee, from the sale of lands in the execution of its said trust, after deducting all costs, charges, and expenses attending such sales, shall constitute a sinking fund for the redemption of said bonds, and shall be faithfully applied to that object.

And it shall be the duty of said second party, on or before the fifteenth day of December, eighteen hundred and eighty, and each ensuing year, to publish in one or more newspapers, in the city of New York, an advertisement setting forth the amount of said sinking fund then on hand, and requesting the holders of said bonds to send written proposals to said second party, specifying the terms respectively for which they would be willing to sell bonds of this series held by them. And said advertisement having been published for sixty days, the trustee shall apply said amount to the purchase of such of said bonds as shall have been offered at the lowest price, provided that the price so to be paid shall not exceed ten per centum premium on the par value of such bonds; but if said bonds cannot be purchased at said rate or at a less rate, it shall be the duty of said second party, without unreasonable delay, to invest the amount on hand, appertaining to said sinking fund, in United States securities, or, with the concurrence of the president and the board of directors of said railway company, in any other securities which the said trustee may select; and all moneys appertaining to the sinking fund which shall come into the hands of said second party from the sales of lands or otherwise shall, for the time being, and until the same can be applied to the purchase of said bonds, or to be invested in stocks as aforesaid, be deposited in one or more of the trust companies in the city of New York, upon the best terms which the said second party, in its reasonable discretion, can obtain for the same.

And when the said several six thousand acres of land for each mile of road built and to be built, hereby conveyed, or intended so

to be, shall be ascertained, surveyed and located, said first party will make schedules and descriptions of the said several sections and parcels of land, from time to time, as the same shall be surveyed and located, and affix thereto the minimum prices at which the same are to be sold.

And said company will furnish said schedules and descriptions duly certified by said railway company, to said second party, together with an affidavit of the president and secretary of the said railway company, that to the best of their knowledge and belief such minimum prices have been affixed, having reference to the relative value of the different sections and parcels of land; and as often as once in each two years the said railway company shall appraise such sections and parcels of land and affix minimum prices thereto as aforesaid, and whenever and so often as such schedule and description of said land shall be made as aforesaid, the same shall be duly acknowledged by said first party, under its corporate seal, and in such manner as to entitle them to be recorded, and shall be duly recorded by said first party in all counties in which said lands may be located; and the description of said lands, when made, shall be deemed and taken as a part of this indenture, with like effect as though said description had been incorporated therein; and whenever said railroad company shall certify, in writing, to said trustee that it has contracted for the sale of any section

31 or parcel of said lands, at a sum not less than the minimum prices affixed to the same, and ten per centum at least of the consideration money shall be paid to said second party, and a bond and mortgage contracted to be sold, in proper form, from the purchaser to the said second party, securing the residue of the consideration money, with the interest thereon, at not less than eight per centum per annum, and payable annually, shall be delivered to the trustee, such mortgage having first been duly acknowledged and recorded, the said second party shall make, execute and acknowledge a deed, conveying to such purchaser, his heirs and assigns, all the right, title, interest, estate and property of the said trustees, of, in and to the section or parcel of land so sold, with a covenant that they have not done any act to defeat or prejudice their title to the land so conveyed; provided, that in all cases the true consideration or price of the land shall be set forth in the conveyance, and shall in no case, except as hereafter provided, be less than the minimum price affixed to the same as aforesaid. Sales may also be made in like manner of any section or parcel of said land, at less than the minimum prices affixed as aforesaid, when the president and secretary of the said railway company shall make and furnish to said trustee an affidavit that the price agreed on is, in his opinion, the full market value of the land so agreed to be sold.

The consideration money, on any such sale of said lands may be paid either in whole or in part, by delivering to said trustee, to be canceled, one or more of this series of bonds which may have been issued by said railway company, as aforesaid, at their par value; and payments upon any such mortgage of the purchaser of any of

said lands may be made by delivering to said trustee one or more said bonds at their par value, amounting in the aggregate to said consideration or purchase money; and two or more purchasers of said lands may unite and pay a part or all of the aggregate amount of consideration money of their purchases, or a part or all of the aggregate amount of their mortgages by delivering to said trustees said bonds to the amount of such payment, to be canceled. And the said second party shall, as often as once in each year, if required by the party of the first part, furnish to said first party a detailed statement of the land sold by them, and also of the moneys and securities in their hands as such trustee, and of such other matters connected with the trusteeship as the party of the first part may reasonably require.

Whenever the said trustee, party of the second part, shall receive any of the bonds above mentioned in payment for lands sold, or on mortgages held by them as such trustee, or by purchase of such bonds as above provided, the same, with any unpaid interest warrants or coupons annexed thereto, shall be immediately canceled, and shall thereafter only be held as vouchers by said trustee.

And the said Houston and Texas Central Railway Company, for itself, its successors and assigns, doth hereby covenant and agree to and with the said second party, its successors and assigns, for the more fully assuring and conveying the said premises and property, and carrying into effect the objects and purposes of this indenture, to make, execute and deliver, all and singular, such further assurances and instruments as shall from time to time be necessary, and as said trustee or its counsel may deem necessary or advisable.

And it is hereby mutually agreed, and these presents are upon the express condition, that, upon the payment of the principal sum and interest of the bonds herein provided for, the estate hereby granted to the said party of the second part shall be void and the right and title to the premises hereby conveyed shall revert to and revest in said party of the first part, its successors and assigns, without any acknowledgment of satisfaction, reconveyance, re-entry or other act.

And the said party of the second part, its successors in said trust and assigns, shall only be accountable for reasonable diligence in the management thereof, and shall not be responsible for the acts of any agent employed by it, when such agent shall have been employed with reasonable discretion; and that the said party of the second part, and its successors in this trust, shall be entitled to reasonable compensation for their services in the management of said trust. The word trustee, as used herein, shall be understood to mean the trustee for the time being, whether original or substitute.

33 In witness whereof, the said party of the first part, in conformity with the order of the board of directors, has caused its official seal, and the signature of William H. Dodge, its president, to be hereto affixed; and the said party of the second part has, in its corporate name and style, by its president, signed the same, and caused its official seal to be appended hereto, thereby

indicating its acceptance of the conveyance and trusts contained in the foregoing indenture.

[L. S.]

W. E. DODGE,
President of the Houston & Texas Central Railway Co.
THE FARMERS' LOAN & TRUST
COMPANY,

[L. S.]

By R. G. ROLSTON, *Pres.*

Attest: GEO. P. FITCH, *Secretary.*

Signed, sealed and delivered in the presence of
J. AUGUSTUS JOHNSON.
WILLIAM H. CLARKSON.

Amended Bill Making George E. Downs Defendant.

Circuit Court of the United States, Eastern District of Texas.

THE FARMERS' LOAN AND TRUST COMPANY,
Complainant,

vs.

THE HOUSTON AND TEXAS CENTRAL RAILWAY
Company *et al.*, Defendants.

No. 227. Equity.

Now comes the complainant, and by leave of the court first had and obtained, amends its original bill and says:

1. That as stated in clause VII of the original bill, George E. Downs, who is a citizen of New York, residing in the city of Brooklyn therein, became the purchaser of all the mortgaged property and premises, set forth and described in said original bill, at a sale thereof made in pursuance of a decree of this court made at the Galveston term thereof in May, 1888, in consolidated cause No. 198, upon the chancery docket of this court, entitled Nelson S. Easton *et al.* vs. The Houston and Texas Central Railway Company *et al.*, and the said Downs so purchased the said property and premises subject in every respect to the lien and mortgage of complainant, as set out in its said original bill, and that the said George E. Downs is a necessary party to this suit;

Wherefore, complainant makes the said George E. Downs a party defendant hereto.

To the end, therefore, that the said defendant Downs may answer the several matters and things hereinbefore stated in complainant's original bill as fully and particularly as if they were herein again repeated (the answer under oath being hereby expressly waived); and the said defendant was thereto specially interrogated, and that the said mortgaged premises may be sold in the manner and for the purposes as in said original bill prayed, the full prayer of which is now here alluded to and adopted; and that complainant may have such other and further relief as its case may require.

May it please your honor- to grant unto complainant an order directing the said Downs to appear, plead, answer or demur by a certain day, to be designated, which order shall be served on the

said Downs, if practicable, wherever found; and in the alternative it prays that if such personal service cannot be had upon the said Downs, that your honors will grant unto complainant an order of publication, giving notice to the said Downs, who is a non-resident, as before stated, of the substance and object of complainant's bill, and warning him to appear in this court, in person or by solicitor, on or before a certain day, to be designated, to appear, plead, answer or demur, and to show cause, if any he has, why a decree ought not to pass as prayed.

And as in duty bound your orator will ever pray, etc.

TURNER, McCLURE & ROLSTON,
WILLIE, MOTT & BALLINGER,

Compl't's Solicitors.

M. F. Mott, one of the solicitors of complainant, being duly sworn, on oath saith that the matters and things set forth in the foregoing amended bill as stated upon knowledge are true, and those stated upon information and belief he believes to be true.

M. F. MOTT.

35 Sworn to and subscribed before me Dec. 3d, 1889.

[SEAL.]

C. DART,

Com'r U. S. Circ't Court, E. D. T.

Indorsements: "No. 227. Equity. The Farmers' Loan and Trust Company *vs.* H. & T. C. R'y Co. *et al.* Amended bill making George E. Downs defendant. Filed Dec'r 3d, 1889. C. Dart, clerk. Turner, McClure & Rolston; Willie, Mott & Ballinger."

Order Appointing Receiver of the Waco and Northwestern Division.

Circuit Court of the United States, Eastern District of Texas.

THE FARMERS' LOAN & TRUST COMPANY

versus

THE HOUSTON AND TEXAS CENTRAL RAILWAY COMPANY ET ALS. }

This cause came on to be heard this sixth day of April, 1889, on the application of complainant for the appointment of one or more receivers.

Present: David McClure, Esq., solicitor for complainant; W. B. Botts, Esq., solicitor for defendants.

Whereupon, and on consideration whereof, the court consenting that said Charles Dillingham, as receiver of the Houston & Texas Central Company, be a party defendant herein; it is ordered, adjudged and decreed by the court that Charles Dillingham, who is already in possession of the Houston & Texas Central lines of railway as receiver, under orders of this court, be, and he is hereby appointed receiver, under the prayer of the bill so filed for the foreclosure of the said Waco and Northwestern Division first mortgage, of all the railway and property which is covered by said mortgage, with power to manage and operate the same, and prosecute and

defend all suits connected therewith, and generally to discharge all the duties of receiver respecting such railway property, and that he be appointed such receiver without giving further bond than that which he has already filed in the consolidated cause.

36 And it is further ordered that said receiver hereafter make and file separate accounts, and make and file his reports and accounts in this cause, keeping and stating the earnings and expenditures of the entire railway property under his charge, so as to show at all times and with all practicable accuracy the separate earnings and expenses of the Waco and Northwestern division of said railway, and that he apply the earnings of said railway in such manner as the court shall from time to time order.

And it is further ordered that all sales of lands belonging to the said Waco and Northwestern division, and covered and affected by the said first mortgage, be conducted in the same manner as the court has already directed with regard to sales of the Houston and Texas Central lands generally in the consolidated cause, and in accordance with the system now in operation, and that the proceeds of such sales be turned over to the trustee, and that the trustee give deeds as has hitherto been done.

And it is further ordered, that said trustee make and file quarterly with the special master, John G. Winter, full and complete statements of all the funds coming into its hands, and of all investments made by it, and all sums expended by it in the administration of its trust, and that the receiver pass his accounts every three months before said John G. Winter, as special master, on due notice and at such time and place as the said master may appoint, and that the said receiver further report to this court at each and every term thereof. The clerk will file this order and the bill of foreclosure in this case, of date April 6th, 1889.

DON A. PARDEE,
Circuit Judge.

April 6th, 1889.

Indorsed: No. 227. Equity. The Farmers' Loan & Trust Co. v. The Houston & Texas Central Railway Co. *et als.* File of date April 6th, 1889. D. A. P. Order appointing receiver. Filed April 6th, 1889. C. Dart, clerk.

37 *Answer of Charles Dillingham, Receiver.*

In the Circuit Court of the United States, Eastern District of Texas.

THE FARMERS' LOAN AND TRUST COMPANY, Complainant,	}
vs.	
THE HOUSTON AND TEXAS CENTRAL RAILWAY COMPANY and Charles Dillingham, as Receiver of the Houston and Texas Central Railway, Defendants.	

The separate answer of Charles Dillingham as receiver of the Houston and Texas Central Railway Company, one of the defendants in suit of The Farmers' Loan and Trust Company, complainant, *vs.* The Houston and Texas Central Railway Company and Charles Dillingham as such receiver, defendants.

Charles Dillingham, as receiver of the Houston and Texas Central Railway Company, one of the defendants in the suit above named, saving and reserving all manner and benefit of exception that can or may be had or taken to the complainant's bill, because of the many errors, imperfections and insufficiencies therein contained, for his separate answer to said bill, or so much thereof as he is advised is necessary for him to answer, answering, says:

First. From information which he believes to be true, he admits that the complainant is a corporation under the laws of the State of New York, but he does not know, nor is he advised, and, therefore, cannot admit, that said corporation is authorized or empowered to receive or hold in trust, lands, railroads, franchises or other property, or to execute trusts, as alleged in the complainant's bill.

Second. He admits that the Houston and Texas Central Railway Company was organized under the laws of Texas, as a railroad corporation, at or about the dates mentioned in complainant's bill, and that by virtue of its corporate powers it acquired its main line and franchises substantially as set forth in paragraph II of complainant's bill.

38 Third. He admits that said railway company, under the laws of Texas, acquired lands to aid in the construction of its main line and several branches substantially as set forth in paragraph III of complainant's bill.

Fourth. He admits, upon information and belief, that said railway company, at or about the dates mentioned in paragraph IV of complainant's bill, made, executed and delivered the several mortgages therein mentioned, each one covering in a general way the railroad and lands specifically named in said paragraph.

Fifth. He admits the filing of the bill by the Southern Development Company, on or about the 16th of February, 1885, and that all the property of said railway company, of every sort and description, was placed by order of this honorable court in the hands of receivers, as therein stated, and that said suit resulted as stated in paragraph V of said bill, except that, as he is informed and believes, an appeal to the Supreme Court of the United States was

taken by the Southern Development Company from the decree of this court thereon, which appeal is still pending and undetermined in said Supreme Court.

He admits that bills in equity were filed in this court by the trustees of the main-line first mortgage, Western Division first mortgage, and a general mortgage for the foreclosure of said mortgages respectively, and proceedings were thereupon had substantially as stated in said paragraph.

Sixth. He admits that after the consolidation of said causes, as stated in paragraph VI of complainant's bill, mortgages were foreclosed substantially as therein stated, and the property conveyed by them decreed to be sold as mentioned in complainant's bill, subject however, to the first mortgage to the complainant on the Waco and Northwestern division.

Seventh. He admits that in pursuance of said decree, the entire property of said railway company was sold *on* or about the time stated in paragraph VII of complainant's bill, and admits and avers that at said sale, all the property and premises, rights, privileges, immunities and franchises of every kind and description, covered by the Waco and Northwestern Division first mortgage to complainant, including the lands as therein stated, was sold by the master commissioner, and purchased by one George E. Downs, and

39 that said sale and purchase was in every respect subject to the lien of the said first mortgage to the complainant on said property but without any personal assumption of the payment of said mortgage on the part of the purchaser. He also admits and avers that a deed thereof has been made and delivered to said Downs as provided by the decree of said court, and that said deed was made subject, in all respects, to the liens of said first mortgage to complainant but without any personal assumption of the payment of said mortgage on the part of the purchaser.

Eight. He admits that Nelson S. Easton and James Rintoul who were appointed receivers with this respondent have been relieved of their duties as such, by an order of this honorable court made in said consolidated cause, and that this respondent, by order of the court, is now in possession as sole receiver, of all the property formerly of said railway company, including the property of every sort and description covered by the Waco and Northwestern Division first mortgage to complainant.

Ninth. This respondent does not admit that complainant's mortgage is a first lien upon the property thereby conveyed, but on the contrary, he avers that the Lackawanna Iron and Coal Company, the Southern Development Company, Morgan's Louisiana & Texas Railroad and Steamship Company, and others claim to be entitled to liens on said property paramount and superior to any lien of said first mortgage to complainant therein, for the particulars of which claims this defendant refers to the claims of intervention heretofore filed by such parties in the said consolidated cause, and which are still pending undetermined therein. He admits that the copy of said mortgage appended to complainant's bill is substantially a true

copy of said original mortgage, so far as he knows or has reason to believe.

Tenth. Respondent admits that said Waco and Northwestern first mortgage was made to secure a series of bonds substantially as stated in paragraph 10 of complainant's bill, and that said bonds were in substance and effect the same as set forth in said paragraph; but as they were issued before this respondent had any connection with the property of said railway company, and having no personal knowledge of said mortgage, he does not know, and, there-
40 fore, cannot admit what number of bonds, if any, have been signed or certified by the complainant, nor what number or amount of them, if any, is now outstanding or unpaid, or entitled to the benefit of the security of said mortgage.

Eleventh. He admits that said mortgage conveys, or purports to convey in trust, all and singular the properties mentioned therein and referred to in paragraph XI of complainant's bill.

Twelfth. He admits that the said mortgage or trust deed contained provisions substantially as set forth in paragraph 12 of complainant's bill.

Thirteenth. He admits that said railway company has made default in the payment of interest on said bonds from the time stated in paragraph XIII of complainant's bill. Whether said Downs has paid all, or any part of said interest, this defendant is not informed and does not know. This respondent is not advised, nor does he know what amount, if any, of interest on said bonds remains overdue or unpaid, as alleged in paragraph XIV of complainant's bill, or what demands may have been made for payment thereof.

Fourteenth. This respondent is not advised, nor does he know what amount, if any, may be due to complainant or bondholders upon, for, or in respect of coupon interest on any such bonds.

Fifteenth. This respondent has no knowledge or information as to any of the matters alleged in paragraphs XV, XVI, XVII, XVIII, XIX and XX, of complainant's bill, except as informed by the allegations in said paragraphs, and, therefore, he is not prepared to admit or deny such allegations, or any of them.

Sixteenth. He neither admits nor denies, but submits to the judgment of the court, the matters set forth by complainant in the paragraph constituting folios 40 and 41, on page 14 of the printed copy of said bill of complaint, being the paragraph immediately following paragraph XX of said bill.

Seventeenth. The respondent further answering, says that at the time of the institution of this suit he had no other relation to, or connection with, or interest in, the property described in the
41 bill of complaint in said suit, and claimed to be covered by the mortgage sought to be foreclosed therein, except as he had been, and was, receiver of the same, together with other property, appointed by this court in the suit of the Southern Development Company, and in the consolidated cause hereinbefore mentioned under orders and decrees of said court in said suits, and that he has now no other or further relation to, or connection with or interest in the same, except as by an order heretofore made in this

suit, his receivership of said property has been extended to this suit; that prior to the time of the institution of this suit all the property of the Houston and Texas Central Railway Company which was covered by the so-called first mortgage to complainant on the Waco and Northwestern division of the Houston and Texas Central railway, had been sold at judicial sale as hereinbefore stated, and duly conveyed to one George E. Downs, who, as this respondent is informed and believes, at the time of such purchase was, and has ever since been, and still is a resident of the city of Brooklyn, in the State of New York, and a citizen of said last-mentioned State. That this respondent prays leave to refer, with the like effect as if the same and the contents and effect thereof were here fully and at large set forth, to the decree for the sale of said property, the proceedings in respect to such sale, the order of confirmation thereof, and the deed of conveyance of the property so purchased by said Downs, and the certificates of record of such deed, and he avers that as he is informed and believes the said Downs duly paid the purchase price of said property so purchased by him, and since about the day of the date of said last-mentioned deed, and since a date long prior to the institution of this suit, has been the sole owner of the said property so purchased by and conveyed to him, and has not in anywise sold or disposed of the same, and this respondent is advised by his counsel that the said Downs is a necessary and indispensable party to any suit for the foreclosure of said so-called first mortgage on the Waco and Northwestern division of the Houston and Texas Central railway, and must be brought in and made a party to said suit before the rendering of any decree for the foreclosure of such mortgage, or any sale of such property.

42 Eighteenth. For greater certainty, and by way of qualification to that extent, if need be, of the admissions hereinbefore in this answer contained, this respondent prays leave to refer to the originals, or duly certified copies of the acts of the legislature, records of proceedings in suit, mortgages, deeds of trust, and other documents in said bill of complaint, or in this answer referred to, with the like effect as if the same and the contents and effect thereof were herein fully and at large set forth.

This respondent, being only the custodian of said property under the orders of this honorable court, and now having fully answered, prays to be hence dismissed with his reasonable costs in this behalf expended, including a reasonable fee for advice and preparation of this answer.

CHAS. DILLINGHAM.

BAKER, BOTTS & BAKER,

Counsel & Sol'rs for Def't Chas. Dillingham.

STATE OF TEXAS,)
Harris County.)

I, Charles Dillingham, one of the defendants in the foregoing cause, having read the foregoing answer, and being duly sworn, do say that the matters and things in said answer contained, as alleged

of my own knowledge, are true, and that those alleged on information I believe to be true.

CHAS. DILLINGHAM.

Subscribed and sworn to before me this 3d day of September, A. D. 1889.

[Seal. 3634/201/2.]

J. C. KIDD,
Notary Public, Harris County, Texas.

Indorsements: "No. 227. Equity. U. S. circuit court, district of Texas. Farmers' Loan and Trust Company against Houston and Texas Central Railroad Company *et al.* Answer of Charles Dillingham, receiver. Filed Sep. 4, 1889. C. Dart, clerk, by W. L. Hanscom, deputy."

43 United States Circuit Court, Eastern District of Texas, at Galveston.

THE FARMERS' LOAN AND TRUST COMPANY	}	No. 227.
<i>against</i>		
GEORGE E. DOWNS, Impleaded with THE HOUSTON & Texas Central Railway Company and Charles Dillingham, as Receiver.		

Separate Answer of George E. Downs.

The defendant, George E. Downs, saving and reserving to himself all benefit and advantage of exception or otherwise to which he may be or become entitled by reason of the manifold errors, uncertainties and insufficiencies of the bill of complaint in the above-entitled suit for answer thereto, or to so much and such parts thereof as he is advised it is material for him to make answer unto, answering, says:

First. He admits and avers that the complainant, at the time of the commencement of said suit, was, and has ever since been, and still is, a corporation created under the laws of the State of New York, and a citizen of said State, having its principal office and place of abode in the city of New York, and that this defendant, at the time of the commencement of said suit, was, and has ever since been, and still is, a citizen of the said State of New York, having his place of abode in the city of Brooklyn, in said State. He is advised and therefore avers, that this court was and is wholly without jurisdiction of this suit or the matters involved therein.

Second. He has no knowledge and is uninformed save by said bill in respect to the other matters alleged in article 1 of said bill, or in respect to any of such matters.

Third. He has no knowledge and is uninformed, save by said bill, as to whether, by act of the legislature of the State of Texas, approved May 24th, 1873, or otherwise, the Waco & Northwestern Railroad Company, or its properties, rights, privileges or franchises, was or were merged in the Houston & Texas Central Railway Com-

pany, or became a part thereof, or whether the Houston & Texas Central Railway Company, by virtue of said acts, or otherwise, or according to law, became a corporation, owning or operating a line from its main line at Bremond to Ross, known as the Waco and Northwestern division, or by any other name, or whether under any acts of the legislature of Texas, or otherwise, the said railway company became entitled to receive any land from the State of Texas for or in respect of the whole or any part of any such line from the main line at Bremond to Ross.

Fourth. He admits, upon information and belief, that at or about the several dates stated, on that behalf in article IV of said bill, the said Houston & Texas Central Railway Company executed certain mortgages or deeds of trust, but prays leave to refer to the originals or certified copies of such mortgages or deeds of trust, for the contents, purport and effect thereof, and denies each and every allegation in said bill contained in respect to the contents, purport and effect thereof, except so far as upon an inspection of the said mortgages or deeds of trust or certified copies thereof, such allegations may be found to be correct and true, and he has no knowledge and is uninformed, save by said bill, as to whether or not the said mortgage or deed of trust, dated June 16, 1873, made to the complainant, did in fact cover the Waco and Northwestern division, so called, or six thousand, or any other number, of acres of land for each mile thereof; and he requires strict proof thereof.

Fifth. He has no knowledge and is uninformed save by said bill as to the allegations in article V or VI of said bill or any of such allegations except that as he is informed and believes that in a consolidated cause pending in this court, wherein Nelson S. Eaton and James Rintoul, trustees, and The Farmers' Loan and Trust Company, trustee, were complainants, and The Houston & Texas Central Railway Company and others were defendants, a decree of foreclosure and sale was entered by this court at the May term thereof held at Galveston on or about May 4, 1888, to which decree of foreclosure or sale or a certified copy thereof he prays leave to refer for the contents, purport and effect of said decree, and he denies each and every allegation in said bill contained in respect

45 to the contents, purport and effect thereof, except so far as upon reference to said decree or a certified copy thereof, the same may be found to be correct and true. He admits and avers that at the sale under such decree all the property of every kind and description covered by the so-called Waco and Northwestern Division first mortgage was offered for sale by the master commissioner appointed by said decree, subject to the said mortgage, but without any personal assumption of the payment of such mortgage on the part of the purchaser, and was purchased by this defendant; and that a deed of the property purchased by this defendant has been made and delivered to him, which deed, or a certified copy thereof, will be produced upon the trial of this cause, and to which deed or a certified copy thereof, this defendant prays leave to refer for the contents, purport and effect thereof. He admits and avers that the property sold by the said master commissioner, and purchased by

this defendant at the sale hereinabove referred to, included lands which were estimated at about 277,220 acres, as stated in the master commissioner's notice, under which such sale was made, and in the deed from the said master commissioner to this defendant, the same being, as this defendant was informed and believes, a portion of the lands described in the said so-called Waco and Northwestern first mortgage, as being lands conveyed thereby; and he avers upon information and belief that such lands so conveyed, or purported to be conveyed, by such mortgage still remain, for the most part, unsold and undisposed of, less than one-third thereof having been heretofore sold, or contracted to be sold; and that the same are of substantial and considerable value; and that the same are the lands in respect to which it is expressly prescribed in said mortgage that they, or so much thereof as may be necessary, shall be first (that is to say prior to the institution of proceedings to procure a decree of sale of any of the mortgaged premises or property), sold by the complainant at public or private sale for the best price which can be obtained for the same, without any legal proceedings whatsoever; but he avers upon information and belief that
46 such lands were not, nor were any of them, so sold prior to the institution of this suit, nor have they, or any of them, been since so sold.

Sixth. He has no knowledge and is uninformed save by said bill as to the allegations contained in subdivision VIII of said bill or any of them.

Seventh. He has no knowledge and is uninformed save by said bill as to the allegations contained in subdivision IX of said bill, or any of such allegations, except that upon information and belief he admits that a substantially correct copy of the so-called Waco & Northwestern first mortgage is annexed to said bill. He does not admit that such mortgage is a first lien upon the property purporting to be covered thereby, but he avers upon information and belief that the Lackawanna Iron and Coal Company, the Southern Development Company and Morgan's Louisiana & Texas Railroad & Steamship Company, and Thomas M. Shirley and others claim to be entitled to liens on said property paramount and superior to any lien of said mortgage to complainant thereon, for the particulars of which claims this defendant refers to the petitions of intervention heretofore filed by some of such parties in the said consolidated cause, and which are still pending undetermined therein, and to the record of proceedings in a suit heretofore instituted by said Shirley against the Houston & Texas Central Railway Company and others, in the district court of McLennan county, in the State of Texas, from which, as this defendant is informed and believes, it appears: That in 1869, the Waco Tap Railroad Company is alleged to have entered into a contract in writing with one Thomas M. Shirley to construct its line of railway, with the exception of furnishing the rails, from its junction with the Houston & Texas Central railway to Waco, a distance of about fifty (50) miles. That on July 16th, 1870, said Shirley filed suit in the district court of McLennan county, Texas, to recover damages, actual and ex-

emplary, for breach of contract, in which suit he alleged that his claim was an equitable lien arising from said alleged contract; that said suit has been tried a number of times, in which large verdicts were rendered, which were appealed. That said suit was tried February 2d, 1875, which resulted in a judgment in favor of said Shirley for \$107,682.95, from which the Waco

47 Tap Railroad Company appealed to the supreme court, and upon hearing the judgment was reversed and the cause remanded. That an amendment was filed April 2d, 1876, making the Houston & Texas Central Railway Company a party defendant; and on November 11th, 1876, a second trial of said suit was had in said district court, which resulted in a judgment for plaintiff for \$100,010.50, from which the Houston & Texas Central Railway Company appealed, and upon hearing the judgment of the district court was reversed and said cause remanded. That on November 10th, 1881, plaintiff again filed an amendment to his petition, in which he made the directors of the Waco & Northwestern Railroad Company parties defendant; and the cause was again tried in said district court October 19th, 1885, which resulted in a verdict and judgment against the Waco & Northwestern Railroad Company in the sum of \$16,453.90 for money and interest found to be due Shirley, and a judgment of foreclosure of his alleged equitable mortgage on the forty-five (45) miles of road from the town of Bremond to the city of Waco; and also for \$96,602 against the Waco & Northwest- Railroad Company as damages, but which claim for damages was declared not to be a lien upon the road. That from this judgment Shirley appealed to the supreme court, and in 1889 said judgment was again reversed and the cause remanded, with instructions to the court below to try the issue whether the sale of the Waco & Northwestern railroad made to the Houston & Texas Central Railway Company was fraudulent as to Shirley's right as a creditor of said Waco & Northwestern Railroad Company, and to try no other issue then made or presented by the pleadings in the case; and if upon a trial of said issue it should be found that said sale was not fraudulent, then, and in that event, judgment should be entered against the trustees (the former directors) for the stockholders and creditors of said Waco and Northwestern Railroad Company, in their representative capacity only, for the sum of \$16,453.90, with interest on said sum from October 19th, 1885, together with a foreclosure of said Shirley's alleged lien upon the railway, and appurtenances thereto belonging, from the town of Bremond to the city of Waco, and that judgment should be

48 rendered against said trustees for the sum of \$96,602, with interest thereon from said October 19th, 1885, to be paid out of any assets in their hands as such trustees. That said court further instructed that if, upon a trial of said issue, it should be found that the sale of the said Waco and Northwestern railroad and its appurtenances was made with the intent to defraud the creditors of said Waco and Northwestern Railroad Company, then, and in that event, the said Waco and Northwestern Railroad Company should be adjudged subject to sale for the satisfaction of the judgment to be

rendered in favor of Shirley against the said trustees. That the case was again tried on the 15th day of October, 1890, and judgment was entered in favor of said Shirley against the surviving trustees of the Waco and Northwestern Railroad Company, in their representative capacity, for the sum of \$24,671.63, with interest at the rate of ten per cent. per annum from that date, together with a judgment for foreclosure of the alleged equitable mortgage on the railroad extending from the town of Bremond to the city of Waco, and upon the road bed and right of way, superstructure, rights, properties and franchises, stated to be in the possession of the defendant, The Houston and Texas Central Railway Company. That it was further adjudged that the plaintiff, T. M. Shirley, should recover from said trustees, in their representative capacity, the further sum of \$135,199.86, which, together with the former sum of \$24,671.62, aggregates the sum of \$159,871.48. That it was further adjudged that the said sale, made by the Waco and Northwestern Railroad Company to the Houston and Texas Central Railway Company, be canceled and set aside as to the rights of the plaintiff Shirley as a creditor of said Waco and Northwestern Railroad Company, and the property so conveyed to the said Houston and Texas Central Railway Company was decreed by the court to be subject to sale for the satisfaction of the aggregate judgment of \$159,171.48; and said alleged equitable mortgage was decreed to be foreclosed, and the sheriff of McLennan county was directed and ordered to enter, seize and levy upon the said railway extending from the town of Bremond to the city of Waco as a whole, and to sell the same as under execution at Waco, McLennan county, for the satisfaction of said aggregate judgment, interest and all costs.

49 Eighth. He has no knowledge and is uninformed save by said bill as to the allegations contained in subdivisions X, XI or XII of said bill, or any of them except so far as such allegations relate to the contents of the so-called Waco and Northwestern first mortgage and of the bonds purporting to be secured thereby, as to which he prays leave to refer to the original of such mortgage and bonds when the same may be produced in this suit.

Ninth. He has no knowledge and is uninformed save by said bill as to the allegations contained in subdivisions XIII, XIV, XV, XVI, XVII, XVIII, XIX and XX, and the unnumbered paragraph at the top of page 14 of the printed bill in this suit, beginning with the words "In consequence of the embarrassed condition" and concluding with the words "shall seem right and equitable to be conferred," or any of such allegations except that he is advised and therefore charges that any trust imposed upon the complainant under the Waco and Northwestern first mortgage can be executed and the rights of all parties ascertained and fully protected in the premises otherwise than by judicial sale of the mortgaged premises.

Tenth. This defendant shows that it doth not appear by the averments of said bill that the complainant is entitled to have a receiver for the rents, revenues or income of said railway; nor does it appear that complainant is entitled to apply the same to the payments of the principal and interest alleged to be due under said mortgage,

wherefore this defendant doth demur to the complainant's right to relief in this respect and to so much of said bill as relates thereto.

Eleventh. Respondent shows and suggests to the court that all the property, rights and franchises of the Houston & Texas Central Railway Company having been sold out, as appears from the complainant's bill, the persons who were directors of said company at the date of said sale became the trustees of such sold-out corporation under the laws of the State of Texas, and as such were at the date of the filing of complainant's bill, and still are, its sole legal representatives, and as such were and are necessary parties to this

50 suit, and that until they are brought in and impleaded there is a defect of parties in the cause and the court cannot proceed to final decree. The following is a list of said directors, all of whom are within the jurisdiction of this honorable court for the purposes of this suit, viz: Alexander C. Hutchinson and J. George Schriever, residents and citizens of the city of New Orleans, State of Louisiana; Collis P. Huntington and Isaac E. Gates, residents and citizens of the city and State of New York; Eber W. Cave, Charles Dillingham, John J. Atkinson, residents and citizens of Harris county, State of Texas; Abraham H. Swanson, a resident and citizen of Corsicana, State of Texas, and Charles Fowler, a resident and citizen of Galveston, in the State of Texas.

And now having fully answered complainant's bill, this respondent prays to be hence dismissed with his reasonable costs in this behalf expended.

GEORGE E. DOWNS,
By ROUSE & GRANT,
His Solicitors.

Indorsements: No. 227. United States circuit court, east dist. Texas. Farmers' Loan and Trust Co. vs. Houston and Texas Cent. Railway Co. *et al.* Answer of Geo. E. Downs. Filed Feb'y 2, 1891. C. Dart, clerk. Rouse & Grant, solicitors.

Replication to Answer of Charles Dillingham.

In the Circuit Court of the United States for the Eastern District of Texas, at Galveston.

THE FARMERS' LOAN AND TRUST COMPANY,	} In Equity. Ch. 227.
Complainants,	
vs.	
THE HOUSTON AND TEXAS CENTRAL RAIL-	} In Equity. Ch. 227.
way Company and Others, Defendants.	

Complainant's replication to separate answer of Charles Dillingham.

This repliant, saving and reserving to itself all, and all manner of advantage of exception to the manifold insufficiencies of the said separate answer of Charles Dillingham, for replication there-
51 unto saith, that it will aver and prove its said bill to be true, certain, and sufficient in law to be answered unto; and that

the said separate answer of the said Charles Dillingham is uncertain, untrue, and insufficient to be replied unto by this repliant; without this, that any other matter or thing whatsoever in the said separate answer contained, material or effectual in the law to be replied unto, confessed and avoided, traversed or denied, is true; all of which matters and things this repliant is, and will be, ready to aver and prove, as this honorable court shall direct; and humbly prays, as in and by its said bill it hath already prayed.

TURNER, McCLURE & ROLSTON,
WILLIE, MOTT & BALLINGER,
Solicitors for Complainant.

Indorsements: No. 227. Equity. U. S. cir. court, east dist. Tex. Farmers' Loan and Trust Co. vs. H. & T. C. R'y Co. *et al.* Replication to answer of Dillingham. Filed Dec'r 20, 1889. C. Dart, clerk.

United States Circuit Court, Eastern District of Texas, at Galveston.

THE FARMERS' LOAN AND TRUST COMPANY	}	No. 227.
vs.		
THE HOUSTON AND TEXAS CENTRAL RAILWAY COMPANY, Charles Dillingham, Receiver, and George E. Downes.		

Replication of The Farmers' Loan and Trust Company, Complainant, to the Separate Answer of George E. Downes.

This repliant, saving and reserving to itself all and all manner of advantage of exception which may be had and taken to the manifold errors, uncertainties and insufficiencies of the answer of the said defendant, George E. Downes, for replication thereto, saith that it doth and will aver, maintain and prove its said bill to be true, certain and sufficient in the law to be answered unto by the said defendant, and that the answer of the said defendant is very uncertain, evasive and insufficient in law to be replied unto by this repliant; without that, that any other matter or thing in the said answer contained, material or effectual in the law to be replied unto, and not herein and hereby well and sufficiently replied unto, confessed or avoided, traversed or denied, is true; all which matters and things this repliant is ready to aver, maintain and prove as this honorable court shall direct, and humbly prays, as in and by its said bill it hath already prayed.

TURNER, McCLURE & ROLSTON AND
WILLIE, MOTT & BALLINGER,
Solicitors for Complainant.

Indorsements: No. 227. Equity. The Farmers' Loan & Trust Co. vs. Houston & Texas Central R'y Co. *et al.* Replication of pl'ff to answer of George E. Downes. Filed Feb'y 13th, 1891. C. Dart, clerk.

Final Decree.

At a regular term of the circuit court of the United States, for the eastern district of Texas, held at the court-rooms, in the city of Galveston, on the 16th day of March, 1892.

Present: The Honorable Don A. Pardee, circuit judge; D. E. Bryant, district judge.

THE FARMERS' LOAN AND TRUST COMPANY,	} In Equity. No. 227.
Complainant,	
<i>vs.</i>	
THE HOUSTON AND TEXAS CENTRAL RAIL-	
way Company, Charles Dillingham, and	
George E. Downs, Defendants.	

This cause came on to be heard at this term upon the pleadings and proof, and was argued by counsel, and thereupon, upon consideration thereof, it is ordered, adjudged and decreed as follows:

I.

It is adjudged and decreed that the mortgage set forth in the bill of complaint made by the Houston & Texas Central Railway Company to the complainant, The Farmers' Loan and Trust Company, bearing date the 16th day of June, 1873, is a valid and subsisting mortgage, and constitutes a first lien upon the mortgaged premises, property, lands and franchises described in said mortgage as follows:

All and singular the railway of the Houston and Texas Central Railway Company, known as the Waco and Northwestern division, built and to be built, beginning at a point on the main line of the Houston and Texas Central railway, passing through the city of Waco, in McLennan county, to the Red river, and thence to the northern boundary line of the State, together with all side-tracks, turnouts, rolling stock, equipment and material, all right of way and tracks, depot and shop grounds, tenements, hereditaments, rights and franchises, including and meaning to include all the property, real and personal, now acquired or which may hereafter be acquired by the said company in the State of Texas, pertaining to the operation of said division, and also all and singular six thousand acres of land per mile of completed road to the said division, said lands to be selected from the ten thousand two hundred and forty (10,240) acres of land per mile of completed road, donated by the State of Texas to aid in the construction of the said Waco and Northwestern railroad, as in said mortgage specified.

II.

Also, that there has been issued under the provisions of said mortgage, one thousand one hundred and forty bonds for one thousand dollars each, with interest coupons attached, and that there are now outstanding of said issue 1,096 bonds, 44 having been hereto-

fore taken up and paid by the trustee with the interest coupons thereon falling due after July 1st, 1891; and that said bonds so outstanding, together with the coupons on said 44 bonds redeemed, as aforesaid, due prior to the 1st day of July, 1891, are secured by a first lien upon all of said property. That there is outstanding the following coupons upon said bonds past due and unpaid upon which are due the following sums, viz:

(1.) The amount of \$39,900 for coupons due January 1, 1886, with interest at the rate of six per centum per annum from that date.

54 (2.) The amount of \$39,900 for coupons due July 1, 1886, with interest at like rate from that date.

(3.) The amount of \$39,900 for coupons due January 1, 1887, with interest at like rate from that date.

(4.) The amount of \$39,900 for coupons due July 1, 1887, with interest at like rate from that date.

(5.) The amount of \$39,900 for coupons due January 1, 1888, with interest at like rate from that date.

(6.) The amount of \$39,900 for coupons due July 1, 1888, with interest at like rate from that date.

(7.) The amount of \$39,900 for coupons due January 1, 1889, with interest at like rate from that date.

(8.) The amount of \$39,900 for coupons due July 1, 1889, with interest at like rate from that date.

(9.) The amount of \$39,900 for coupons due January 1, 1890, with interest at like rate from that date.

(10.) The amount of \$39,900 for coupons due July 1, 1890, with interest at like rate from that date.

(11.) The amount of \$39,900 for coupons due January 1, 1891, with interest at like rate from that date.

(12.) The amount of \$39,900 for coupons due July 1, 1891, with interest at like rate from that date.

(13.) The amount of \$38,260 for coupons due January 1, 1892, with interest at like rate from that date.

(14.) The amount of \$1,096,000 for principal of said bonds not yet due with interest coupons thereon from January 1, 1892. Making the amount due for interest up to March 15th, 1892, the sum of \$618,982.75 and the further amount of \$1,112,900 owing upon the unmatured bonds.

III.

Also, that by a decree of foreclosure and sale in consolidated cause No. 198, in equity, on the docket of this court, wherein Nelson S. Easton and James Rintoul, trustees, and The Farmers' Loan and Trust Company, trustee, were complainants, and The Houston and Texas Central Railway Company and others were defendants, entered by the court on the 4th day of May, 1888, the property, premises and franchises covered by the mortgage set out and described in the bill of complainant herein, were ordered sold subject to the first lien of complainant; and that at said sale the property
55 of every kind and description covered by said mortgage was purchased by the defendant, George E. Downs, and a deed

thereof was made and delivered to him. That the purchase so made by said Downs was made subject in all respects to the lien of complainant's mortgage on said property, and that in said deed it is expressly stated that the same was made subject in all respects to the said lien.

IV.

Also, that the property covered by said mortgage consists of the railway of the Houston and Texas Central Railway Company, beginning at a point on the main line of said railway company in the town of Bremond, in Robertson county, Texas, passing through the county of Falls and running to the town of Ross, in McLennan county, in said State, a distance of about fifty-eight miles, together with all side tracks, turnouts, rolling stock, equipment and materials, all right of way and tracks, depot and shop grounds, tenements, hereditaments, rights and franchises including all the property, real and personal, pertaining to the operation of the said fifty-eight miles of railway, and including the franchise to build to the Red river, and thence to the northern boundary line of said State; and also about 277,230 acres of land, donated by the State of Texas, in aid of the construction of said railway.

V.

It is further ordered and decreed that unless the defendant, George E. Downs, shall, on or before the expiration of thirty days from the entry of this decree, pay into the registry of this court for the use and benefit of the holders of the unpaid coupons secured by the mortgage aforesaid, dated the 16th day of June, 1873, the following sums, namely:

(1.) A sufficient sum of money to pay the costs of complainant in this cause as they shall be taxed and its compensation and counsel fees, as fixed by this court, and (2) the amount of the unpaid coupons due on said mortgage bonds, as aforesaid, all as hereinbefore stated, then the said mortgaged premises shall be sold as hereinafter directed and all right and equity of redemption of the defendant, in and to the said mortgaged premises, property, rights, assets and franchises, and every part and parcel thereof, shall be forever barred and foreclosed.

VI.

It is further ordered and decreed that if default be made in making either of said payments within thirty days, then all the said mortgaged premises and property, real, personal and mixed, rights and franchises wherever situated, shall be sold in the manner and upon the terms hereinafter described. The railway, side tracks, turnouts rolling stock, equipment and materials, all right of way and tracks, depot and shop grounds, tenements, hereditaments, rights and franchises, including all real and personal property pertaining to the operation of said railway, and said lands donated by the State of Texas, including the franchise to build to the Red river and thence to the northern boundary of the State of Texas, shall be sold as an

entirety. Said sale shall be for cash and for the further considerations set forth in the XIV paragraph of this decree and without appraisement or right of redemption, at public auction, to the highest bidder therefor, at twelve o'clock noon, at the front door of the United States court-house, in the city of Waco, in the State of Texas, on a day to be named by the master commissioner herein appointed in his notice of sale. Before making said sale the master commissioner shall publish notice thereof in some newspaper of general circulation in each of the following cities, namely, in the city of New York, in the State of New York, and in the city of Waco, in the State of Texas. Said notice shall be published once in each week for eight weeks; the first publication shall be at least eight weeks before the day of sale, and the notice shall state the time, place and terms of sale, and shall contain a brief description of the property and premises hereby ordered to be sold. The master commissioner making such a sale may either personally or by some person to be designated by him and to act in his name and by his authority, and at the joint request of complainant and the defendant, George E. Downs, adjourn the sale from time to time, without further advertisement, but only on said joint request or by order of the court or a judge thereof.

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VII.

The said master commissioner shall not receive a bid for such property from any person or party unless he or it shall, at or prior to the time of making such bids, deposit or have deposited with the said master commissioner the sum of \$100,000, or a duly certified check satisfactory to the said master commissioner for such amount as the bidder's deposit.

Upon such property being struck off by the said master commissioner to any such bidder at such sale, the said sum of \$100,000, or such certified check so deposited by such bidder, shall be held by said commissioner to the credit of this cause, subject to the order of this court therein.

Any and all deposits made by bidders or intended bidders at such sale, to whom the property may not have been struck off thereat, shall forthwith upon the striking off of the property to another bidder, or at the adjournment of the sale without striking off the property to any bidder, be returned to the depositor thereof. If any sale for which a deposit is made as aforesaid shall not be confirmed by the court, such deposit shall be returned to the bidder. In addition to the bidder's deposit so made by the purchaser at or prior to the time of bidding, such further portions of the purchase price of the property shall be paid in cash and deposited subject to the order of this court as the court in this cause may from time to time direct—the court reserving the right to resell in this cause the premises and properties herein directed to be sold upon the failure of the purchasers thereof, or their successors or assigns, to comply within twenty days with any order of the court in that regard; and in case of any resale or the failure of the purchaser or purchasers to comply with the terms of the bid or the orders of the court rela-

tive to such additional partial payments as may from time to time be directed, all sums deposited or paid in by such purchaser or purchasers shall be forfeited as a penalty for such non-compliance. The balance of the purchase price may be paid either in cash or in the bonds, or the overdue coupons secured by the mortgage—each such
 58 bonds and coupons being received for such sums as the holder thereof would be entitled to receive under the distribution herein ordered.

VIII.

It is further ordered, the parties consenting thereto, and convenience being thereby subserved and expenses diminished, that Christopher Dart be and he is hereby designated and appointed as master commissioner to make the sale hereby ordered and decreed, and to execute and deliver a deed of conveyance of the property so to be sold to the purchaser or purchasers thereof, on the order of the court, or a judge thereof confirming such sale. The court reserves the right, however, in term time or at chambers to appoint another person such master commissioner with like powers, in case of the death or disability to act of the master commissioner hereby designated, or in case of his resignation, or failure to act, or removal by the court.

IX.

It is further ordered and decreed that within thirty days from the confirmation of said sale, or such further time as the court may allow on the application of the purchaser or purchasers, for good cause shown, the purchaser, or purchasers of said property shall complete payment of the entire amount of the bid to the said master commissioner; on such payments, the said purchaser or purchasers shall be entitled to receive a deed of conveyance thereof from the master commissioner and from the other parties to this suit as herein provided, and to receive the possession of the property so purchased from the defendants, George E. Downs and Charles Dillingham, receiver, who shall thereupon make delivery of the same. On such payment being made the master commissioner shall publish for ten days in some newspaper published in the city of New York a notice fixing the time when and the place where he will be ready to pay the said mortgage bonds, or coupons entitled to be paid out of the proceeds of sale.

X.

It is further ordered and decreed that the fund to arise from said sale shall be applied as follows:

- 59 (1.) To the payment of such portion of the costs of this suit as this court or a judge thereof may subsequently determine, and also to the compensation of the complainant herein for its services, charges and expenses in the execution of its trust, including its own compensation, and its disbursement, expenses and charges for solicitors' and counsel fees in the execution of its said trust; also the compensation of the receivers and his counsel and

all proper expenses attendant upon the sale of the property, including the compensation of the commissioner making such sale, all of which charges and expenses shall be thereafter fixed and allowed by the court, or a judge thereof.

(2.) To the payment of the said mortgage coupons, and interest thereon to the amounts hereinbefore specified, or if the funds be not sufficient to pay the same, then the said said coupons with interest thereon shall be paid *pro rata*.

(3.) To the payment of the unmatured bonds and interest thereon, or if the fund be not sufficient to pay the same in full, then the said bonds with interest thereon shall be paid *pro rata*. Each of the said bonds and coupons presented to him shall be stamped by the said master commissioner so as to show the amount that has been paid on same, and on account of the coupon interest due thereon, and returned so stamped to the holder thereof. In case of payment in full of said bonds and coupons with interest thereon, the same shall be delivered with payment in full stamped thereon by the master commissioner to the purchaser as a muniment of title.

(4.) If, after making all of the above payments, there shall be any surplus, the same shall be paid according to the further order of the court in that regard.

XI.

It is further ordered and decreed that the defendant, George E. Downs, and the complainant, The Farmers' Loan and Trust Company, and each of them, be and they are hereby authorized and directed to execute and deliver under the direction of the master commissioner conveyances executed by the said parties respectively

60 by way of confirmation and further assurance of title to the said purchaser or purchasers, his, its or their assigns, of all and singular the mortgaged property and premises and every part or parcel thereof of every kind and description and wherever situated, herein directed to be sold by the master commissioner. The forms of said conveyance and the mode of execution shall be settled and approved by the master commissioner, or by the court, if any question should arise as to the form or sufficiency thereof, and such conveyance shall be delivered to such purchaser, or purchasers, his, its or their assigns, contemporaneously with the deed or deeds of the master commissioner.

XII.

It is further ordered and decreed that without any further application or petition, John G. Winter, Esq., the special master in chancery herein, is directed to examine as soon as possible and report to the court on or before the rule day in August, 1892, the compensation to be allowed to the complainant and its counsel and solicitors, to the receiver in this cause and his counsel, and to the master commissioner, and in making these examinations he shall hold sittings in Texas, and may also hold sittings in New York, as the convenience of the parties and the master may require.

XIII.

It is further ordered and decreed that when delivery is made by the receiver of the property herein ordered to be sold to the purchaser or purchasers, he shall pass his final accounts before the special master.

XIV.

It is further ordered and decreed that the purchaser or purchasers of the property herein and hereby ordered to be sold shall be vested with and shall hold, possess and enjoy the said mortgaged premises, privileges and franchises appurtenant thereto as fully and completely as the said George E. Downs, defendant herein, now holds or enjoys, or at the time of the commencement of this suit held and enjoyed, or is or was entitled to hold or enjoy; and further, that the purchaser or purchasers shall have and be entitled to hold
61 said railroad and property free and discharge from the claims of all parties to this suit. And the purchaser or purchasers of said property at said sale shall, as a part of the consideration of the purchase, and in addition to the sum bid, take the property upon the express condition that he or they will pay off, satisfy and discharge any and all claims and interventions now pending and undetermined in this court, accruing prior to the appointment of the receiver herein or during the receivership, which may be allowed and adjudged by this court as prior in right to complainant's mortgage, together with such interest as may be allowed; and also upon the further express conditions that he or they will pay off, satisfy and discharge all debts, claims and demands of whatsoever nature incurred or which may hereafter be incurred by said receiver, Charles Dillingham, and which have not been or shall not hereafter be paid by said receiver or other parties in interest herein; and said purchaser or purchasers, their successor or successors, or assigns, shall also have the right to appear and make defence to any claim, debt or demand sought to be enforced against said property; and said purchaser or purchasers, their successor or successors, or assigns, shall also have the right to appear and make defence to any claim, debt or demand pending and undetermined at the date of the confirmation of such sale. All claims, debts and demands accruing during the receivership herein shall be barred unless presented by intervention in this cause within six months after the confirmation of said sale; and jurisdiction of this cause is retained by this court for the purpose of enforcing the provisions of this article of this decree.

And it is further ordered, adjudged and decreed that it be recited in the deed to be executed and delivered to said purchaser or purchasers, that he or they do take said property, subject to, and that said purchaser or purchasers do assume and agree to pay off any and all debts, claims, and demands of whatsoever nature now pending and undetermined, and which may be allowed and adjudged by this court, as prior to any right secured under complainant's mortgage, and subject likewise to all debts, claims and demands of what-

62 soever nature incurred by Charles Dillingham as receiver in this cause, and which may remain unpaid at the termination of said Dillingham's receivership, provided the same be presented, as hereinbefore provided, within six months after the confirmation of said sale.

XV.

It is further ordered, adjudged and decreed that the rights of the Lackawanna Coal and Iron Company, the Southern Development Company, the Pacific Improvement Company, and the Morgan's Louisiana & Texas Railroad and Steamship Company, intervenors herein, and the rights of all other intervenors herein be and they are hereby reserved to be hereinafter adjudicated, and are in no manner affected or prejudiced by this decree. It is further ordered that the disposition of any surplus funds arising from the earnings of the road, or otherwise, that may be in the hands of the receiver, is reserved for future determination.

XVI.

And it is further ordered, adjudged and decreed, that any party to this cause, and also any intervening petitioner who has filed his petition herein, and also the receiver, may at any time apply to this court for further relief at the foot of this decree, as well as for such modifications thereof in respect to the distribution of the proceeds of sale as equity may require.

In open court this 16th day of March, A. D. 1892.

DON A. PARDEE,

Circuit Judge.

DAVID E. BRYANT,

Dist. Judge.

Indorsements: No. 227. Equity. The Farmers' Loan and Trust Company, trustee, *vs.* The Houston & Texas Central Railway Co. *et al.* Final decree. Filed March 16th, 1892. C. Dart, clerk. A true copy.

Petition to Amend Final Decree and Order Thereon. Filed May 16, 1892.

THE FARMERS' LOAN AND TRUST COMPANY, Complainants, }

vs.

HOUSTON AND TEXAS CENTRAL RAILROAD COMPANY, CHARLES Dillingham, and George E. Downs, Defendants. }

63 In the Circuit Court of the United States for the Eastern District of Texas, at Galveston. In Equity.

The petition of The Farmers' Loan & Trust Company, complainant herein, respectfully represents that by the 7th clause of the final decree of foreclosure, rendered herein on the 16th day of March, 1892, it was provided that no person should make a bid at the sale unless at or prior to the time of making such bid he should deposit

or have deposited with the said master commissioner the sum of one hundred thousand (\$100,000) dollars, or a duly certified check therefor, satisfactory to said master commissioner.

That by the terms of said decree any party to this cause has the right to apply for further relief at the foot thereof.

That the requirement of said section 7 is a hardship in that no person can make a bid unless such deposit shall have been first made. And your petitioner says that this will have the effect of preventing a competition at the sale. That either to procure certified check, or the cash amounting to one hundred thousand (\$100,000) dollars will entail expense and trouble, for which the bidder will not be reimbursed if the property is not adjudged to him. That the safeguards for the purpose of preventing improvident bids will be fully accomplished if the amount is reduced, which will in the opinion of petitioner encourage competition at the sale.

The premises considered, the petitioner prays that the said section 7 of the said final decree be so amended as to allow the master commissioner to receive bids upon a deposit of twenty-five thousand (\$25,000) dollars, being made either in cash or by duly certified check. And petitioner further says that if in the opinion of the court it should be necessary to further protect the property from improvident bids it suggests that a further deposit of twenty-five thousand (\$25,000) dollars shall be made by the party to whom the property is struck off before the sale shall be confirmed.

And petitioner prays for such other and further relief in the premises as in equity it may be entitled.

64

Order.

This cause came on to be heard this 14th day of May, 1892, before Don A. Pardee, circuit judge, and was argued by M. F. Mott, Esq., for complainant, and Wm. Grant for defendants, whereupon the court considering the foregoing petition, and being fully advised in the premises, it is further adjudged and decreed that section 7 of the final decree entered in this cause on the 16th day of March, 1892, be amended so as to read as follows:

VII.

The said master commissioner shall not receive a bid for such property from any person or party unless he or it shall at or prior to the time of making such bid deposit or have deposited with the said master commissioner the sum of \$25,000 or a duly certified check satisfactory to the said master commissioner for such amount as the bidders deposit.

Upon such property being struck off by the said master commissioner to any such bidder at such sale, the said sum of \$25,000, or such certified check so deposited by such bidder, shall be held by said commissioner to the credit of this cause, subject to the order of this court therein.

Any and all deposits made by bidders or intended bidders at such

sale, to whom the property may not have been struck thereat, shall forthwith upon the striking off of the property to another bidder, or at the adjournment of the sale without striking off the property to any bidder, be returned to the depositor thereof. If any sale for which a deposit is made as aforesaid shall not be confirmed by the court, such deposit shall be returned to the bidder. In addition to the bidder's deposit so made by the purchaser at or prior to the time of the bidding, such further portions of the purchase price of the property shall be paid in cash and deposited subject to the order of this court as the court in this cause may from time to time direct, the court reserving the right to resell in this cause the premises and properties herein directed to be sold upon the failure of the purchasers thereof or their successors or assigns to comply within twenty days with any order of the court in that regard; and in case of any resale or the failure of the purchaser or purchasers to comply with the terms of the bid or the orders of the court relative to such additional partial payments as may from time to time be directed, all sums deposited or paid in by such purchaser or purchasers shall be forfeited as a penalty for such non-compliance. The balance of the purchase price may be paid either in cash or in the bonds or the overdue coupons secured by the mortgage—each such bonds and coupons being received for such sums as the holder thereof would be entitled to receive under the distribution herein ordered.

DON A. PARDEE,
Circuit Judge.

Indorsements: "No. 227. Equity. The Farmers' Loan and Trust Co. *vs.* The Houston & Texas Central Railway Co. *et al.* Petition to amend final decree and order thereon. Filed May 16, 1892. C. Dart, clerk."

Order Amending Final Decree. Filed May 16, 1892.

United States Circuit Court, Eastern District of Texas. (At Chambers.)

FARMERS' LOAN AND TRUST COMPANY	}	No. 227.
<i>vs.</i>		
THE HOUSTON AND TEXAS CENTRAL RAILWAY CO., GEO. E. DOWNS, <i>et al.</i>		

It appearing to the court that there was error in the final decree of the court rendered herein on the 16th day of March, 1892, as to the amount due complainant, it is now ordered, all parties in interest assenting thereto, that the second clause of said decree be and the same is amended so as to read as follows:

II.

Also, that there has been issued under the provisions of said mortgage one hundred and forty bonds of one thousand dollars each, with interest coupons attached, forty-four of which, with the

interest coupons thereto, have heretofore been taken up
 66 and paid by the trustee; and that of said bonds there are
 now outstanding 1,096, which, with the interest due thereon,
 are secured by a first lien upon all said property. That there is
 now due upon outstanding, past-due and unpaid coupons of said
 1,096 bonds, and upon said bonds, the following sums, to wit:

1. The amount of \$38,360 for coupons due January 1, 1886, with interest at the rate of six per cent. per annum from that date.....	\$38,360 00
2. The amount of \$38,360 for coupons due July 1, 1886, with interest at like rate from that date..	38,360 00
3. The amount of \$38,360 for coupons due January 1, 1887, with interest at like rate from that date..	38,360 00
4. The amount of \$38,360 for coupons due July 1, 1887, with interest at like rate from that date..	38,360 00
5. The amount of \$38,360 for coupons due January 1, 1888, with interest at like rate from that date..	38,360 00
6. The amount of \$38,360 for coupons due July 1, 1888, with interest at like rate from that date..	38,360 00
7. The amount of \$38,360 for coupons due January 1, 1889, with interest at like rate from that date..	38,360 00
8. The amount of \$38,360 for coupons due July 1, 1889, with interest at like rate from that date..	38,360 00
9. The amount of \$38,360 for coupons due January 1, 1890, with interest at like rate from that date..	38,360 00
10. The amount of \$38,360 for coupons due July 1, 1890, with interest at like rate from that date..	38,360 00
11. The amount of \$38,360 for coupons due January 1, 1891, with interest at like rate from that date..	38,360 00
12. The amount of \$38,360 for coupons due July 1, 1891, with interest at like rate from that date..	38,360 00
67	
13. The amount of \$38,360 for coupons due January 1, 1892, with interest at like rate from that date	38,360 00
14. The sum of \$15,983.33 for accruing interest on the amount of said 1,096 bonds from January 1st, 1892, to March 15, 1892....	15,983 33
15. The amount of \$1,096,000 owing on said 1,096 bonds not yet due..	1,096,000 00
16. Making in all:	
For past-due coupons and interest thereon.....	594,675 90
For accruing interest on the principal of said bonds from January 1, 1892, to March 15, 1892.....	15,983 33
For principal of said bonds...	1,096,000 00
	<hr/>
	\$1,706,659 23

Done and signed this 14th day of May, 1892.

DON A. PARDEE,

Circuit Judge.

Indorsements: "No. 227. Equity. The Farmers' Loan and Trust Co vs. The Houston and Texas Central Railway Co. et al. Order amending final decree. Filed May 16, 1892. C. Dart, clerk. A true copy.

Master Commissioner's Report of Sale.

In the Circuit Court of the United States for the Eastern District of Texas, at Galveston.

THE FARMERS' LOAN AND TRUST COMPANY,
Complainant,

vs.

THE HOUSTON AND TEXAS CENTRAL RAILWAY
Company, Charles Dillingham, and George
E. Downs, Defendants.

No. 227. Equity.

To the honorable the judges of said court:

The undersigned master commissioner, duly appointed by the decree in said cause, entered on the 16th day of March, 1892, at the regular March term of said court, in the city of Galveston, Texas, begs leave respectfully to report:

That in accordance with said decree, he caused notices to be published in the "Evening Post," a daily newspaper published in the city of New York, and in the "Waco Daily Globe," and in the "Waco Daily Day and Globe," successor to the "Waco Daily Globe," newspapers of general circulation, published respectively in the city of New York, and in the city of Waco, in the State of Texas, a notice that he would, on the 28th day of December, 1892, or the day to which he might adjourn the said sale, at 12 o'clock, noon, at the front door of the United States court-house, in the city of Waco, in the State of Texas, make sale at public auction, to the highest bidder therefor, of all the mortgaged premises and property, real, personal and mixed, rights and franchises, wherever situated, mentioned in said decree and thereby directed to be sold, viz:

"The railway of the Houston and Texas Central Railway Company, beginning at a point on the main line of said railway company in the town of Bremond, in Robertson county, Texas, passing through the county of Falls, and running to the town of Ross, in McLennan county, in said State, a distance of about fifty-eight (58) miles, together with all side tracks, turnouts, rolling stock, equipment and materials, all right of way and tracks, depot and shop grounds, tenements, hereditaments, rights and franchises, including all the property, real and personal, pertaining to the operation of the said fifty-eight (58) miles of railway, and including the franchise to build to the Red river, and thence to the northern boundary line of said State. And, also, about two hundred and seventy-seven thousand, two hundred and thirty (277,230) acres of land, donated by the State of Texas in aid of the construction of said railway."

The said notices further gave notice that the said property would be sold in the manner and upon the terms hereinafter described, viz:

The railway, side tracks, turnouts, rolling stock, equipment and materials, all right of way and tracks, depot and shop grounds, tenements, hereditaments, rights and franchises, including all
 69 real and personal property pertaining to the operation of said railway, and said lands donated by the State of Texas, including the franchise to build to the Red river, and thence to the northern boundary of the State of Texas, would be sold as an entirety. That the said sale would be for cash, and for the further considerations hereinafter stated, and without appraisalment or right of redemption.

Reference was also made in said notices that for further details of the respective properties to be sold, reference was made to said decree and the schedules on file with the clerk of said court, at Galveston, Texas, subject to the inspection of all intending bidders at such sale.

Said notices further gave notice that in addition to the bidder's deposit of twenty-five thousand (\$25,000.00) dollars, required in said decree to be made by the bidder with the master commissioner before the bid of such bidder should be received, the purchaser at, or prior to the time of the bidding, such further portions of the purchase price of the property should be paid in cash, and deposited subject to the order of this court, as the court in this cause might from time to time direct, the court reserving the right to resell, in this cause, the premises and properties in said decree directed to be sold, upon the failure of the purchasers thereof, or their successors or assigns, to comply within twenty (20) days with any order of the court in that regard, and in case of any resale, or the failure of the purchaser or purchasers to comply with the terms of the bid, or the orders of the court relative to such additional partial payments, as might from time to time be directed, all sums deposited or paid in by such purchaser or purchasers should be forfeited as a penalty for such non-compliance. That the balance of the purchase price might be paid either in cash or in the bonds, or the overdue coupons secured by the mortgage, each such bonds and coupons being received for such sums as the holder thereof would be entitled to receive under the distribution herein ordered.

That within thirty (30) days from the confirmation of such sale, or such further time as the court might allow on the application of the purchaser or purchasers for good cause shown, the purchaser or
 70 purchasers of said property shall complete payment of the entire amount of the bid to the said master commissioner; on such payment the said purchaser or purchasers should be entitled to receive a deed of conveyance for the property sold from the master commissioner, and from the other parties to this suit, as provided in said decree, and to receive the possession of the property so purchased from the defendants, George E. Downs and Charles Dillingham, receiver, who shall thereupon make delivery of the same.

That the purchaser or purchasers of the property in said decree ordered to be sold, shall be vested with, and shall hold, possess and enjoy the said mortgaged premises, privileges and franchises appurtenant thereto, as fully and completely as the said George E. Downs,

defendant herein, now holds or enjoys, or at the time of the commencement of this suit held and enjoyed, or is or was entitled to hold or enjoy; and, further, that the purchaser or purchasers shall have and be entitled to hold said railroad and property, free and discharged from the claims of all parties to this suit.

And that the purchaser or purchasers of said property at said sale shall, as a part of the consideration of the purchase and in addition to the sum bid, take the property upon the express condition that he or they will pay off, satisfy and discharge any and all claims and interventions now pending and undetermined in this court accruing prior to the appointment of the receiver herein, or during the receivership which may be allowed and adjudged by this court as prior in right to complainant's mortgage, together with such interest as may be allowed; and, also, upon the further expressed conditions that he or they will pay off, satisfy and discharge all debts, claims and demands of whatsoever nature incurred, or which may hereafter be incurred by said receiver, Charles Dillingham, and which have not been, or shall not hereafter be paid by said receiver or other parties in interest herein.

The said notices further contain the provision that it shall be recited in the deed to be executed and delivered to said purchaser or purchasers, that he or they do take said property subject to, and that said purchaser or purchasers do assume and agree to pay off any and

71 all debts, claims and demands of whatsoever nature now pending and undetermined, and which may be allowed and adjudged by this court as prior to any right secured under complainant's mortgage, and subject, likewise, to all debts, claims and demands of whatsoever nature incurred by Charles Dillingham as receiver in this cause, and which may remain unpaid at the termination of said Dillingham's receivership, provided the same be presented, as provided in said decree, within six (6) months after the confirmation of said sale.

The said notices further contained a recital that the rights of The Lackawanna Iron and Coal Company, The Southern Development Company, The Pacific Improvement Company, and The Morgan's Louisiana and Texas Railroad and Steamship Company, intervenors herein, and the rights of all other intervenors herein are reserved to be hereinafter adjudicated, and are in no manner affected or prejudiced by said decree.

The said notices were published in said newspapers once a week for eight (8) weeks, and the first publication in each of said papers was made at least eight (8) weeks before the day appointed for said sale, to wit: the 28th day of December, 1892.

Copies of said notices so published in said newspapers are hereto annexed, and marked respectively "A" and "B," and are made part of this report of sale.

The said master commissioner further begs leave to report that in accordance with said decree, and with the said notices, he attended, in the city of Waco, in the State of Texas, on the said 28th day of December, 1892, and at 12 o'clock, noon, the day and hour named in said notices, at the front door of the United States court-

house, in the said city of Waco, in the State of Texas, and made sale of all the mortgaged property, premises and franchises hereinbefore described, at public auction to the highest bidder for cash, and for the further considerations as set forth in said decree and in said notices; and at said sale, after crying the said property for a reasonable time, and receiving various bids therefor, the said master commissioner received a bid from E. H. R. Green for the sum of one million three hundred and seventy-five thousand dollars (\$1,375,000),

72 which bid being the highest bid received from any person, after full and public notice given by said master commissioner at said sale, all of said property hereinbefore described was struck off to the said E. H. R. Green as the purchaser thereof, and the said E. H. R. Green was then and there publicly declared by said master commissioner the purchaser at said sale of all the property, premises and franchises hereinbefore described.

The said master commissioner further reports that in accordance with said decree, before receiving the bid of the said E. H. R. Green, or of the other parties bidding at said sale, to wit: L. Harrison, J. Kruttschnitt and William T. Gould, each of said persons deposited with said master commissioner a certified check for the sum of twenty-five thousand (\$25,000.00) dollars. That immediately after said sale the certified checks deposited by the said William T. Gould, L. Harrison and J. Kruttschnitt were returned to them by the said master commissioner, and their receipts taken therefor. That the certified check deposited by the said E. H. R. Green was by said master commissioner deposited for collection, and the amount thereof, twenty-five thousand (\$25,000.00) dollars, deposited with the assistant treasurer of the United States at New Orleans, La., to the credit of the said master commissioner in said cause, subject to the order of this court.

The said master commissioner begs leave respectfully to report that before any bids were received for said property Hon. George Clark, as attorney for the stockholders of the Waco and Northwestern Railway Company, their representatives and assigns, gave public notice as to the land granted by the State of Texas to said railway company, which notice is hereunto annexed, marked "C." Also, before said sale, E. A. McKenney, as attorney for T. M. Shirley *et al.*, also gave public notice at said sale in respect to a judgment alleged to have been recovered by the said T. M. Shirley, of and from the surviving trustees of the Waco & Northwestern Railroad Company, in the district court of McLennan county, Texas. The said notice is hereunto annexed, marked "D."

Respectfully submitted.

C. DART,
Master Commissioner.

Notice Published in "Evening Post."

Commissioner's sale.

In the Circuit Court of the United States for the Eastern District of Texas, at Galveston.

THE FARMERS' LOAN AND TRUST COM-
pany, Trustee, Complainant,

vs.

THE HOUSTON & TEXAS CENTRAL
Railroad Company, Charles Dilling-
ham, and George E. Downs, De-
fendants.

No. 227. Chancery Docket.

Notice is hereby given that, in pursuance of a decree entered in the above-entitled cause, on the 16th day of March, 1892, at the regular March term of said court, in the city of Galveston, Texas, I, the undersigned master commissioner thereby designated, shall on the 28th day of December, 1892, or the day to which I may adjourn such sale, at twelve o'clock noon, at the front door of the United States court-house, in the city of Waco, in the State of Texas, make sale at public auction to the highest bidder therefor, of all the mortgaged premises and property, real, personal and mixed, rights and franchises wherever situated, mentioned in said decree and thereby directed to be sold, viz:

The railway of the Houston and Texas Central Railway Company, beginning at a point on the main line of said railway company in the town of Bremond, in Robertson county, Texas, passing through the county of Falls, and running to the town of Ross, in McLennan county, in said State, a distance of about fifty-eight miles, together with all side tracks, turnouts, rolling stock, equipment and materials, all right of way and tracks, depot and shop grounds, tenements, hereditaments, rights and franchises, including all the property, real and personal, pertaining to the operation of the said fifty-eight miles of railway, and including the franchise to build to the Red river, and thence to the northern boundary line of said State; and also about two hundred and seventy seven thousand, two hundred and thirty (277,230) acres of land, donated by the State of Texas in aid of the construction of said railway.

The same will be sold in the manner and upon the terms herein after described, viz: The railway, side tracks, turnouts, rolling stock, equipment and materials, all right of way and tracks, depot and shop grounds, tenements, hereditaments, rights and franchises, including all real and personal property pertaining to the operation of said railway, and said lands donated by the State of Texas, including the franchise to build to the Red river and thence to the northern boundary of the State of Texas, shall be sold as an entirety. Said sale shall be for cash, and for the fur-

ther consideration hereinafter stated, and without appraisalment or right of redemption.

For further details of the respective properties to be sold reference is hereby made to said decree, and to schedules on file with the clerk of said court at Galveston, Texas, subject to the inspection of all intending bidders at such sale.

The master commissioner will not receive a bid for such property from any person, or party, unless he or it shall, at or prior to the time of making such bids, deposit, or have deposited, with the said master commissioner the sum of \$25,000, or a duly certified check satisfactory to the said master commissioner for such amount as the bidder's deposit. Upon such property being struck off by the said master commissioner to any such bidder at such sale, the said sum of \$25,000, or such certified check so deposited by such bidder shall be held by said commissioner to the credit of this cause, subject to the order of this court therein.

Any and all deposits made by bidders or intended bidders at such sale to whom the property may not have been struck off thereat, shall forthwith upon the striking off of the property to another bidder, or at the adjournment of the sale without striking off the property to any bidder, be returned to the depositor thereof.

If any sale for which a deposit is made as aforesaid shall not be confirmed by the court, such deposits shall be returned to the bidder. In addition to the bidder's deposit so made by the purchaser at or prior to the time of the bidding, such further portions of the purchase price of the property shall be paid in cash and deposited subject to the order of this court as the court in this cause may from time to time direct; the court reserving the right to resell in this cause, the premises and properties herein directed

75 to be sold upon the failure of the purchasers thereof, or their successors or assigns, to comply within twenty days with any order of the court in that regard, and in case of any resale or the failure of the purchaser or purchasers to comply with the terms of the bid or the orders of the court relative to such additional partial payments as may from time to time be directed, all sums deposited or paid in by such purchaser or purchasers shall be forfeited as a penalty for such non-compliance. The balance of the purchase price may be paid either in cash or in the bonds, or the overdue coupons secured by the mortgage, each such bonds and coupons being received for such sums as the holder thereof would be entitled to receive under the distribution herein ordered.

Within thirty days from the confirmation of said sale, or such further time as the court may allow on the application of the purchaser or purchasers, for good cause shown, the purchaser or purchasers of said property shall complete payment of the entire amount of the bid to the said master commissioner; on such payments, the said purchaser or purchasers shall be entitled to receive a deed of conveyance thereof from the master commissioner and from the other parties to this suit as provided in said decree, and to receive the possession of the property so purchased from the defendants

George E. Downs, and Charles Dillingham, receiver, who shall thereupon make delivery of the same.

The purchaser or purchasers of the property herein and hereby ordered to be sold shall be vested with and shall hold, possess and enjoy the said mortgaged premises, privileges and franchises appurtenant thereto as fully and completely as the said George E. Downs, defendant herein, now holds or enjoys, or at the time of the commencement of this suit held and enjoyed, or is or was entitled to hold or enjoy; and further, that the purchaser or purchasers shall have and be entitled to hold said railroad and property free and discharged from the claims of all parties to this suit. And the purchaser or purchasers of said property at said sale shall as a part of the consideration of the purchase, and in addition to the sum bid,

76 take the property upon the express condition that he or they will pay off, satisfy and discharge any and all claims and interventions now pending and undetermined in this court accruing prior to the appointment of the receiver, herein, or during the receivership, which may be allowed and adjudged by this court as prior in right to complainant's mortgage, together with such interest as may be allowed; and also upon the further express conditions that he or they will pay off, satisfy and discharge all debts, claims and demands of whatsoever nature, incurred, or which may hereafter be incurred, by said receiver, Charles Dillingham, and which have not been or shall not hereafter be paid by said receiver or other parties in interest herein.

It shall be recited in the deed to be executed and delivered to said purchaser or purchasers that he or they do take said property, subject to, and that said purchaser or purchasers do assume and agree to pay off, any and all debts, claims and demands of whatsoever nature now pending and undetermined, and which may be allowed and adjudged by this court, as prior to any right secured under complainant's mortgage, and subject likewise to all debts, claims and demands of whatsoever nature incurred by Charles Dillingham as receiver in this cause, and which may remain unpaid at the termination of said Dillingham's receivership, provided the same be presented as provided in said decree within six months after the confirmation of said sale.

The rights of The Lackawanna Iron and Coal Company, The Southern Development Company, The Pacific Improvement Company, and The Morgan's Louisiana and Texas Railroad and Steamship Company, intervenors herein, and the rights of all other intervenors herein, are reserved, to be hereinafter adjudicated, and are in no manner affected or prejudiced by said decree.

Galveston, Texas, October 25th, 1892.

C. DART, *Master Commissioner.*

TURNER, McCLURE & ROLSTON,

22 William Street, New York,

M. F. MOTT, *Galveston, Texas,*

Plaintiff's Attorneys.

77

"B."

Same notice published in "Waco Daily Globe," and in the "Waco Daily Day and Globe," successor to the "Waco Daily Globe."

"C."

To whom it may concern :

The stockholders of the Waco and Northwestern Railway Company, including The City of Waco, through their accredited representatives, hereby give public and formal notice, before sale by C. Dart, special master, that they (said stockholders) are the legal and equitable owners of all the lands granted by the State of Texas to said railway company, including the lands proposed to be now sold, which ownership they (said stockholders) intend to assert in the courts of the country; and that none of said lands belong, either at law or in equity, to the Houston and Texas Central Railway Company.

All parties, and especially such as may contemplate purchasing said lands at the present sale, are notified that no title to said lands will pass by said sale to any purchaser, and that suit will be entered at once against any purchaser, or his vendee or assignee, by said stockholders of the Waco and Northwestern Railway Company through their accredited representatives.

Waco, Texas, December 28th, 1892.

GEO. CLARK,

*Att'y for the Stockholders of the Waco & Northwestern
Railway Company, Their Representatives and Assigns.*

"D."

As the attorney for T. M. Shirley, and others in interest, as plaintiff, I now give notice to purchasers of the Waco and Northwestern railroad, now known as the Waco and Northwestern branch of the Houston and Texas Central railway, at this pending sale of the same: That said T. M. Shirley recovered of and from the surviving trustees of said Waco & Northwestern Railroad Company, to which judgment the said Houston & Texas Central Railway Company is a party, on October 31, 1890, in the district court of McLennan county, Texas, a judgment aggregating then in amount one hundred and fifty-nine thousand eight hundred and seventy-one and $\frac{1}{10}$ (\$159,871.48) dollars. Of which said sum \$24,671.62 is an equitable mortgage on the road, road-bed, right of way, superstructure, &c., of said Waco & Northwestern railroad. And the remaining \$135,199.86 is a judgment lien on said road, road-bed, right of way, superstructure, &c., of the Waco & Northwestern railroad, said cause numbered 1779 in said court.

And said judgment vacates, sets aside and nullifies the sale and transfer of said Waco & Northwestern railroad to the Houston & Texas Central Railway Company, made under a deed of trust executed by John T. Flint, as president of said Waco & Northwestern Railroad Company, to Gray & Botts, trustees, as to the rights of

T. M. Shirley, plaintiff, and orders the sale of said property to satisfy said judgment.

Said judgment is now pending on appeal by the Houston & Texas Central Railway Company and others, before the third division of the court of civil appeals, at Austin, Texas, but no supersedeas bond was given by appellant, and said judgment is not suspended or superseded by said appeal.

This judgment has not been heretofore or now enforced, because the property of said Waco & Northwestern Railroad Company has been, and is now, held by the U. S. circuit court at Galveston, Texas, through its receiver, at the time of its rendition and ever since, though execution or order of sale has issued from said district court of McLennan county, Texas, each year since said October 31, 1890. Waco, Dec'r 28th, 1892.

E. A. McKENNEY,
For T. M. Shirley et al.

Endorsed: "No. 1779. T. M. Shirley vs. Waco Tap R'y Co. Notice to purchasers at sale under decree U. S. court, 1st bonds."

Indorsements: "No. 227. Equity. Farmers' Loan and Trust Co., trustees, vs. Houston and Texas Central Railway Co. et al. Master commissioner's report of sale. Filed January 11th, 1893. C. Dart, clerk, by Geo. H. Burnett, deputy."

565 *Order Appointing Alfred Abeel Receiver in Equity Cause No. 227.*

In the United States Circuit Court, Eastern District of Texas, Fifth Circuit, at Galveston.

THE FARMERS' LOAN AND TRUST COMPANY	}	No. 227. In Equity.
vs.		
THE HOUSTON AND TEXAS CENTRAL RAIL- way Company et al.	}	

Order.

Charles Dillingham, Esq., heretofore appointed receiver in this cause of all the property of the defendant company, having resigned as such receiver, and his resignation having been accepted,

It is ordered that Alfred Abeel, Esq., of Waco, Texas, be, and he is hereby appointed receiver in this case, and is required to give bond as such receiver in the sum of twenty thousand dollars, payable and conditioned as was required in the original order appointing a receiver in this case, with good and sufficient sureties, to be approved by the Hon. David E. Bryant, United States district judge for the eastern district of Texas; and upon the giving of said bond, and its approval and filing with the clerk of this court at Galveston, said receiver Alfred Abeel shall have and exercise all the rights and powers, and discharge all the duties conferred and imposed by law and the previous orders of this court, in this case, on the receiver herein.

And no formal surrender of the custody or delivery of possession of any property, funds, assets, books, vouchers or other thing held by the outgoing receiver shall be necessary, but this order shall operate to put said receiver Abeel in the lawful custody thereof, and all depositories, bailees, officers or employes having the actual custody of any of such property, funds, assets, books, vouchers or other thing held by said outgoing receiver as such, and all persons connected with the operation of the Waco and Northwestern railroad in any manner, shall hold the same for said receiver Abeel, and subject to his authorized directions and orders in reference thereto.

Said receiver Alfred Abeel, shall immediately cause to be made out a detailed statement and inventory of all the property and effects coming into his custody under this order, and make report thereof to the court. He shall also report fully the present condition of said railroad, the Waco, Northwestern, and its rolling stock, and other equipment. He shall make monthly returns of all the operations of said railroad under his charge to the court, filing the same with the clerk at Galveston.

Said receiver is required and is hereby ordered to pay into the registry of this court all the surplus funds now accumulated in the hands of the outgoing receiver, and by this order transferred to said Abeel as receiver, and the clerk shall forthwith deposit the same to the credit of this court in the United States subtreasury at New Orleans.

In chambers, December 6th, 1892.

A. P. McCORMICK,
Circuit Judge.

Indorsements: "No. 227. Equity. The Farmers' Loan and Trust Company, trustee, vs. The Houston and Texas Central Railway Company *et al.* Order appointing Alfred Abeel receiver. Filed Dec. 7th, 1892. C. Dart, clerk."

572 *Petition of Geo. E. Downs as to Funds and Order — Reference Thereon. Filed Oct. 22, '95.*

In the United States Circuit Court for the Eastern District of Texas.

THE FARMERS' LOAN & TRUST COMPANY	} No. 227.
<i>vs.</i>	
THE HOUSTON & TEXAS CENTRAL RAILWAY COMPANY, George E. Downs, <i>et al.</i>	

To the honorable the judges of the United States circuit court for the eastern district of Texas:

The petition of George E. Downs, who has been impleaded and is a defendant in the above entitled cause, respectfully represents that by the eleventh clause of the original decree herein, of March 16th, 1892, and the tenth clause of the amended decree of March 5th, 1895, his right to claim the net earnings of the Waco & North-

western railway was reserved to him, and that said railway was sold under said decrees on the 3d day of September, 1895, and that this court is now in a position to finally determine said claims.

And now your petitioner, for the purpose of propounding his said claims, shows and avers to the court :

573 First. That he purchased said railway and the land grant belonging thereto and all appurtenances, on the 8th day of September, 1888, under the final decree in the case of Nelson S. Easton and James Rintoul, trustees, and The Farmers' Loan & Trust Company, trustee, No. 198, on the docket of this honorable court, subject to the mortgage foreclosed in this cause, but without assuming the payment of the mortgage debt, and paying therefor the sum of twenty-five thousand dollars (\$25,000) in cash at the moment of adjudication, substantially as set forth in the complainant's bill herein, and became in law entitled to the possession and the revenues of the property from the date of his said purchase.

Second. That Charles Dillingham and Nelson S. Easton and James Rintoul remained in possession of said railway and appurtenances under appointment of this honorable court in said suit No. 198, as joint receivers from the date of your petitioner's purchase until December 7th, 1888, when the said Easton and Rintoul were discharged and said Charles Dillingham was continued therein as sole receiver and remained in possession of said railway under his said appointment until the bill in this cause was filed, on or about the 18th day of April, 1889, and your petitioner avers that the aforesaid possession of the said receivers was merely formal and continued for the purpose of closing up their trust and in the interest of and for the benefit of your petitioner as purchaser aforesaid. And petitioner avers that during said period said railway made large net earnings, exceeding in amount the sum of fifty thousand dollars (\$50,000), which in law and equity belong to your petitioner as owner.

Third. Petitioner further shows that the receivership of said Charles Dillingham in said cause No. 198 continued until the bill in this case was filed, on or about the 18th day of April, 1889, when said Charles Dillingham was appointed receiver under the bill filed in this cause. And petitioner avers that at the time of such appointment the said Charles Dillingham had in his hands net earnings derived from the operation of said railway as aforesaid, which amount was taken up by him in his accounts as receiver in this cause and transferred to the present receiver, Alfred Abeel,

574 who now holds the same under the orders of this honorable court, or has deposited the same in the registry of the court, where it is under the orders of this court.

Fourth. Petitioner further shows that said railway has made large net earnings while operated by said receivers, since the date of the filing of the bill in this cause, the exact amount of which the petitioner cannot state, but exceeding, as your petitioner is informed and believes and so avers, the sum of two hundred and seventy-five thousand dollars (\$275,000). And that said amount is in the registry of the court, or in the hands of the present receiver, Alfred

Abeel, subject to the control and disposition of this honorable court.

Fifth. Petitioner further shows that the complainant is not of right, nor by any stipulation contained in the mortgage foreclosed herein, nor by the decree of foreclosure, nor by any order or thing contained in the record of this cause entitled to have the said net revenues, or any part thereof, applied to the payment of the bonds and coupons secured by said mortgage; but, on the contrary, that said net earnings made before the filing of the bill in this case, and subsequent thereto, belong to your petitioner as owner of said railway and land grant, and should be ordered paid over to him.

Petitioner therefore prays that the court may be pleased to order an account to be taken of said net earnings before some suitable person to be appointed master herein for that purpose, and that said master may be directed to find and report specially: First, the net earnings of said railway made between September 8th, 1888, and the date of the filing of the bill in this case, and what portion thereof has come into the hands of the receivers appointed in this cause and what disposition has been made of the same; second, the net earnings made by said railway from the date of the filing of the bill in this case to the date of the sale of said railway, September 3rd, 1895; third, what portion of said earnings has been used for the permanent improvement and betterment of said railway by order of court during said period; fourth, the amount taken from said earnings and applied to the payment of costs and for other purposes by order of court, or otherwise; and that the
575-586 court may be pleased to decree that said net earnings be paid over to your petitioner in accordance with his rights in the premises.

Petitioner further prays that an order be entered directing this petition to be heard upon a day to be fixed, after due notice to all parties in interest, and that the said earnings in dispute may be ordered retained in the registry of the court, or in the hands of the receiver, until this petition can be finally heard and determined; and petitioner prays for costs and all general relief in the premises.

GEORGE E. DOWNS,

By WM. GRANT,

His Solicitor.

Let the foregoing petition be filed and let the complainant and other parties in interest plead to the same within thirty days, and when at issue let the petition be referred to W. L. Prather, Esq., master, with directions — examine into the matter and find and report to the court the facts as specially prayed in said petition.

It is further ordered that the fund claimed by petitioner be retained until said petition can be heard and determined.

It is further ordered that the master file his report under this reference on or before the 1st Monday in January, 1896.

A. P. McCORMICK, *Cir. Judge.*

D. E. BRYANT, *Dist. Judge.*

Indorsements: "No. 227. Eq. Farmers' Loan and Trust Co. vs. Houston & Texas Central R'y Co. et al. Petition of Geo. E. Downs for order as to funds, etc. Filed Oct. 22, 1895. C. Dart, clerk."

587

Int. No. 78.

Master's Report on Petition of Geo. E. Downs, Intervenor.

Filed January 6, 1896.

THE FARMERS' LOAN AND TRUST COMPANY,	}	No. 227. In Equity.
Trustee,		
vs.		
THE HOUSTON & TEXAS CENTRAL RAILWAY		
Company et al.		

588 Intervention of George E. Downs. Filed herein on October 22, 1895.

Master's No., 69.

Findings of Fact by Special Master Wm. L. Prather on Reference to Him of the Above Intervention.

In the Circuit Court of the United States for the Eastern District of Texas, at Galveston.

To the honorable judges of said court :

George E. Downs, intervenor, filed his petition herein on October 22, 1895, and the same was referred to the master by order dated October 22, 1895, with directions to examine into the matter and find and report to the court the facts as specially prayed in said petition, leave being granted at the same time to complainant and other parties in interest to plead to said petition within thirty days from the date of said order, and the master being directed to file his report in said reference on or before the first Monday in January, 1896.

On November 16, 1895, the intervenors, Moran Brothers and Henry K. McHarg, filed their answer to the petition of George E. Downs before the master, and on November 25, 1895, the complainant filed its answer to said petition with the clerk of this court, and the same was filed before the master November 26, 1895.

After notice duly extended to all parties in interest said reference came on to be heard at the United States court-room in Galveston on December 4, 1895, when and where appeared Wm. Grant, Esq., solicitor for intervenor, M. P. Mott, Esq., solicitor for complainant, and L. W. Campbell, Esq., solicitor for Moran Brothers and Henry K. McHarg.

The evidence was heard in part at Galveston on December 4, 1895, and by agreement of all parties the hearing was adjourned to Houston, Texas, where on December 6, 1895, said hearing was concluded.

I file herewith the pleadings of the parties, the list of the evidence introduced, and a memorandum of the hearing at Galveston and Houston.

Upon consideration of the pleadings of the parties and the evidence I submit the following as my conclusions of fact:

589

I.

I find that the evidence fails to show any net earnings arising from the operation of the Waco & Northwestern division of the Houston & Texas Central Railway Company from the date of the intervenor's purchase of said division on September 8, 1888, to the filing of the bill in this cause on April 6, 1889, and it fails to show that either of the receivers in this cause have ever come into possession of any funds arising from the operation of said division during said period.

II.

I find that the earnings arising from the operation of the said Waco & Northwestern railway from April 6, 1889, the date of the filing of the bill in this cause, to September 3, 1895, the date of the sale, amount to \$161,902.51. Included in said amount is \$22,297.06 net land receipts. The gross amount of land receipts is \$38,509.23, of which Alfred Abeel received \$6,383.57 from Chas. Dillingham, former receiver, and of which said gross amount there was derived as rent from land leases the sum of \$13,935.74, and from interest on land deposits the sum of \$667.37, and from land notes the sum of \$14,426.83, and from interest on land notes the sum of \$2,971.49, and from land notes and interest since March 5, 1895, the date of final decree the sum of \$124.23. There has been paid out of said gross amount of land receipts, taxes to the amount of \$14,830.97, and for general land expenses the sum of \$1,372.20.

III.

I find that \$46,505.40 of said net income has been paid out by the receiver under orders of this court since April 6, 1889, up to September 3, 1895, for permanent improvements on the property and for betterments, as set forth in the tabulated statement furnished by the receiver in evidence before me, marked Exhibit T, herewith filed, and returned into court.

IV.

I find that \$52,841.74 of said net income has been paid out
590 by the receiver under orders of this court, since April 6, 1889, to pay costs in this cause, attorney's fees and other court expenses as shown by said tabulated statement.

V.

I further find that of said net income, there remains in the hands of the receiver, or deposited in the registry of the court, the sum of \$362,855.37, after deducting said disbursements, which is subject to the order of this court.

At the instance of the solicitor of intervenors, Moran Brothers and Henry K. McHarg, I make the following additional findings:

I.

I find that intervenor purchased the Waco & Northwestern division of the Houston & Texas Central Railway Company and its land grant under the decree of foreclosure entered in consolidated cause No. 198 on the docket of this court, and that such purchase was made on September 8, 1888, intervenor paying therefor \$25,000.00, which was paid in cash by intervenor at the time of his said bid.

II.

I find that it is provided in the decree of foreclosure entered in said cause No. 198, under which the intervenor purchased, that the sale of the Waco and Northwestern division was sold in all things subject to the prior lien and mortgage given on said division by the Houston & Texas Central Railway Company on June 16, 1883, being the same mortgage declared on herein.

III.

I find that intervenor did in fact purchase said road in all things subject to said first mortgage, and that his said purchase was duly reported to this court by the master commissioner, and said sale was on December 4, 1888, in all things confirmed by this court, and deed was thereafter on the 18th day of January, 1889, made by the master commissioner and delivered to intervenor for said property.

591

IV.

I find that the complainant's mortgage declared on herein, being the same mortgage referred to above, contains the following provision: "And in case the said Houston & Texas Central Railway Company shall fail to pay the principal, or any part thereof, or any instalment of the interest or any part thereof, on any of the said bonds at any time when the same shall become due and payable, according to the tenor thereof, and for sixty days after having been demanded, it shall be competent for said trustee, its successors or assigns, to enter upon the said railway and the premises and property herein conveyed, by its attorneys and agents and take possession of the same without let or hindrance of the said first party, and every part and parcel thereof and the appurtenances, and appoint an agent to operate and manage the same, and receive the revenue and income thereof, applying the said fund after deducting taxes, necessary expenses and counsel fees to keep the same in good order and repair, and the surplus to pay the interest and principal of all the bonds which may be due and outstanding and secured hereby, *pro rata* and thereafter to the payment of any contributions due to the sinking fund herein established; and upon the request of the holders of one-fifth in amount of the bonds so in default, which may be at any time

outstanding under this deed of trust, it shall be the duty of said second party, by its president or agent duly appointed in its behalf to enter upon and take actual possession, with or without entry or foreclosure of said railway and property herein described, and all and singular each and every part and parcel thereof, and assume its management until the arrears of both principal and interest be paid, or the property sold as herein prescribed, receiving the rents, revenues and income thereof, and applying them in the same manner as above stated."

All of which is respectfully submitted.

WM. L. PRATHER,
Special Master.

Indorsements: "Int. No. 78. Farmers' Loan and Trust Company, trustee, vs. H. & T. C. R'y Co. *et als.* No 227. Eq. Geo. E. Downs, intervenor. Report of Wm. L. Prather, special master. Filed January 6, 1896. C. Dart, clerk, by Geo. H. Burnett, deputy."

592 ORIGINAL EXHIBIT T, Substituted by Corrected Statement, Marked "T." Filed January 6th, 1896.

Waco & Northwestern railroad—Alfred Abeel, receiver.

Statement.

Earnings to Aug. 31, 1895, as per sheet.	\$1,672,830 91	
Expenses to Aug. 31, 1895, as per sheet.	2,368,254 19	
		<hr/> \$304,576 72

Income from Operation.

Court expenses as per sheet 3.....	\$52,841 74	
Betterments " " " 4.....	46,505 40	
		<hr/> 99,347 14
Total court expenses and betterments.....		
Net income.....		<hr/> \$205,229 58

Receipts from other Sources.

From Chas. Dillingham, receiver.....	\$100,000	
From Chas. Dillingham, receiver, balance.....	17,731 17	
From Chas. Dillingham, receiver, land act.....	6,383 57	
From land notes & leases.....	15,719 39	
From int. on land deposit....	667 37	
From land notes collected since 3, 5, '95	124 23	
		<hr/> \$140,625 73
On hand and in registry Aug. 31, 1895.....		\$345,855 31
Net earnings, Sept. 1 to 3, 1895, inclusive, as per sheet 5.....		526 01
		<hr/> \$346,381 32

593 Waco & Northwestern R. R., Dec. 3, 1895, auditor's office.
Correct:

S. L. WERDEN,
Act'g Auditor.

Waco & Northwestern railroad—Alfred Abceel, receiver.

Earnings from Operations, Dec. 10, 1892, to Aug. 31, 1895.

Freight	137,053 56	
	29,109 06	
	3,891 65	
	230,796 77	
	89,980 04	
	<hr/>	190,831 08
Passenger	47,239 39	
	4,559 13	
	2,058 38	
	61,902 61	
	31,585 80	
	<hr/>	147,345 31
Mail	4,290 33	
	5,298 69	
	2,917 82	
	972 61	
	<hr/>	13,479 45
Baggage	756 01	
	634 96	
	313 65	
	86 12	
	<hr/>	1,790 74
Express	1,865 00	
	2,090 00	
	1,320 00	
	<hr/>	5,275 00
Rentals	3,743 33	
	4,369 34	
	2,720 00	
	<hr/>	10,832 67
594 Miscellaneous	32 00	
Int. on deposit	3,244 66	
	<hr/>	3,276 66
		<hr/>
		8672,830 91

Correct:

S. L. WERDEN,
Act'g Auditor Waco & Northwestern R. R.

Dec. 3, 1895. Auditor's office.

(1.)

Waco & Northwestern railroad—Alfred Abeel, receiver.

Operating Expenses, Dec. 10, 1892, to August 31st, 1895.

Conducting transportation.....	77,864 81	
	72,366 10	
	31,524 93	
	9,881 04	
	180 36	
	<hr/>	191,817 24
Maintenance of way & structures.....	35,265 50	
	35,235 11	
	13,986 43	
	5,344 88	
	<hr/>	89,831 92
General expense.....	28,046 44	
	24,959 96	
	16,643 63	
	<hr/>	69,650 03
Maintenance of equipment	3,817 33	
	110 88	
	29 83	
	4,824 56	
	4,108 96	
	1,370 68	
	<hr/>	14,262 24
Taxes	420 83	
	9,661 58	
	391 33	
	<hr/>	10,473 74
	<hr/>	
Total expenses.....		376,035 17
595 Less court expenses charged herein by error as follows :		
Brooks & Wallace, printing court record.	149 75	
Clarke & Courts, printing court record..	732 75	
C. Dart, clerk, court costs.....	2,698 48	
E. H. Graham, all'ee as gen. att'y.....	4,200 00	
	<hr/>	7,780 98
		<hr/>
		\$368,254 19

Correct :

S. L. WERDEN,

Act'g Auditor Waco & Northwestern R. R.

Dec. 3, 1895. Auditor's office.

(2.)

Waco & Northwestern railroad—Alfred Abeel, receiver.

Paid for Court Expenses, Dec. 10, 1892, to Aug. 31, 1895.

Farmers' Loan & Trust Co....	\$3,690 96
M. F. Mott	6,000 00
C. Dart, master commissioner....	1,000 00
Turner, McClure & Ralston.....	9,000 00
	<hr/>
	\$22,690 96
W. L. Prather, special master.....	500 00
J. G. Winter, " "	3,850 00
J. G. Winter, " "	150 00
W. L. Prather, " "	500 00
" " " "	750 00
Stenographer to " "	85 00
W. L. Prather, " "	1,000 00
Brooks & Wallace, printing court record.....	22 00
C. Dart, clerk, court costs.....	33 75
" " " "	2,698 48
Brooks & Wallace, printing court record.....	149 75
Clarke & Courts, " " " "	732 75
E. H. Graham, all'ce as gen'l att'y	4,200 00
596 Alfred Abeel, " receiver.....	14,850 00
A. P. McCormick, " gen'l att'y	629 05
	<hr/>
	\$52,841 74

Correct:

S. L. WERDEN,
Act'g Auditor Waco & Northwestern R. R.

Dec. 3, 1895. Auditor's office.

Waco & Northwestern railroad—Alfred Abeel, receiver.

Betterments and Additions, Dec. 10, 1892, to Sept'r 3rd, 1895.

Bridges	\$6,253 85
Shops and round-house.....	1,843 10
Car shed	1,287 80
Water station	50 79
Locomotives.....	18,140 50
Chair car..	6,270 00
Fencing	12,659 36

Total	\$46,505 40
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Correct:

S. L. WERDEN,
Act'g Auditor.

Waco & Northwestern R. R. Dec. 3, 1895. Auditor's office.

Waco & Northwestern railroad—Alfred Abeel, receiver.

Earnings and Operating Expenses, Sept. 1st to 3rd, 1895, Inc.

Freight figured from billing	\$1,162 49
Passenger 1-10 of month of Sept.....	474 36
Mail 1-10 " " " "	48 63
Express 1-10 " " " "	16 50
Extra baggage 1-10 of month of Sept.....	4 20
Rentals 1-10 " " " "	31 50
<hr/>	
Total earnings	\$1,737 68

597

Operating Expenses.

Maintenance of way & S. 1-10 of month of Sept..	\$404 83
Maintenance of equipment 1-10 of month of Sept.	65 66
Conducting transportation 1-10 of month of Sept.	632 35
General expense 1-10 of month of Sept.....	108 83
<hr/>	
	1,211 67

Net earnings Sept. 1 to 3, '95, inc..... \$526 01

Correct :

S. L. WERDEN,

Act'g Auditor Waco & Northwestern R. R.

Dec. 3, 1895. Auditor's office.

Waco & Northwestern railroad—Alfred Abeel, receiver.

Earnings and Operating Expenses for the Month of September, 1895.

Gross earnings.	Total this month.
Passenger	4,743.65
Mail	486.30
Express	165.00
Extra baggage	42.09
Freight.....	32,456.70
Rental	315.00
<hr/>	
Total	38,208.74
Operating expenses	12,116.86
<hr/>	
Net earnings	26,091.88

RECAPITULATION.

Operating Expenses.

Maintenance of way and structures	4,048.32
Maintenance of equipment ...	656.68
Conducting transportation	6,323.51
General expenses.....	1,088.35
<hr/>	
Total ...	12,116.86

Correct :

S. I. WERDEN,

Act'g Auditor.

598

Waco & N'hwestern R. R.

Statement of Freight Earnings from Sept. 1st to 3rd, Inclusive (1895).

From—	To—	
W. & N. W.....	Foreign lines.....	494 85
".....	Local.....	195 21
Foreign lines.....	W. & N. W.....	403 28
	Intermediate.....	69 15

Total..... 1,162 49

Waco, Texas, Dec. 1, '95.

S. L. WERDEN,

Act'g Aud'r.

H.

Indorsements: Original Exhibit T, substituted by corrected statement marked "T I." Int. No. 78. Filed January 6, 1896. C. Dart, clerk, by Geo. H. Burnett, deputy.

"EXHIBIT T I."

Corrected Statement of Earnings, Expenses, &c., from Dec. 10, 1892, to Sept. 3, 1895.

Filed Jan'y 6, 1896.

Waco & Northwestern railroad—Alfred Abeel, receiver.

Statement of Earnings & Expenses, Dec. 10, 1892, to Sept. 3, 1895.
1895.

Aug. 31. Gross earnings from operations as per sheet 1.....	\$689,702 46	
Aug. 31. Expenses of operation as per sheet 2.....	368,354 19	
Income from operation to Aug. 31, 1895.....		321,348 27
Paid for court expenses as per sheet 3...	52,541 74	
Paid for betterments as per sheet 4.....	46,505 40	
599 Total court expenses & betterments.....		99,047 14
Net income to Aug. 31, 1895.....		222,301 13

Received from Other Sources.

From Charles Dillingham, former re- ceiver.....	117,731 17	
From land account as per sheet 5.....	22,297 06	
Total from other sources.....		140,028 23

Total on hand to Aug. 31, 1895.....	362,329 36	
Net earnings, Sept. 1 to 3rd, inc. (1895), as per sh. 6.	526 01	

Total to Sep. 3rd, 1895..... \$362,855 37

Correct:

C. A. RICHARDSON.

Waco & Northwestern railroad—Alfred Abeel, receiver.

Earnings from Operation, Dec. 10, 1892, to Aug. 31, 1895.

Freight	\$137,053 56	
	29,109 06	
	3,891 65	
	230,796 77	
	89,980 04	
	<hr/>	\$490,831 08
Passenger	47,239 39	
	4,559 13	
	2,058 38	
	61,902 61	
	31,585 80	
	<hr/>	147,345 31
600 Mail.....	4,290 33	
	5,298 69	
	2,917 82	
	972 61	
	<hr/>	13,479 45
Baggage.....	756 01	
	634 96	
	313 65	
	86 12	
	<hr/>	1,790 74
Express.....	1,865 00	
	2,090 00	
	1,320 00	
	<hr/>	5,275 00
Rentals.....	3,743 33	
	4,369 34	
	2,720 00	
	<hr/>	10,832 67
Miscellaneous	32 00	
	13,842 32	
	62 84	
	2,304 89	
Int. on deposit	3,244 66	
Right-of-way rents.....	661 50	
	<hr/>	20,148 21
		<hr/>
		\$689,702 46

Correct:

C. A. RICHARDSON.

Sheet 1.

Waco & Northwestern railroad—Alfred Abeel, receiver.

Operating Expenses, Dec. 10, 1892, to Aug. 31st, 1895.

Conducting transportation...	\$77,864 81	
	72,366 10	
	31,524 93	
	9,881 04	
	180 36	
	<hr/>	191,817 24
601 Maintenance of way and structures.....	35,265 50	
	35,235 11	
	13,986 43	
	5,344 88	
	<hr/>	89,831 92
General expense.....	28,046 44	
	24,959 96	
	16,443 63	
	<hr/>	69,450 03
Maintenance of equipment.....	3,817 33	
	110 88	
	29 83	
	4,824 56	
	4,108 96	
	1,370 68	
	<hr/>	14,262 24
Taxes	420 83	
	9,661 58	
	391 33	
	<hr/>	10,473 74
Total expenses.....		\$375,835 17
Less court expenses charged herein by error as follows:		
Brooks & Wallace, printing court record.	\$149 75	
Clarke & Courts, printing court record..	732 75	
C. Dart, clerk, court costs	2,698 48	
E. H. Graham, att'y as gen. att'y... ..	3,900 00	
	<hr/>	7,480 98
Total.....		\$368,354 19

Correct :

C. A. RICHARDSON.

Sheet 2.

Waco & Northwestern railroad—Alfred Abeel, receiver.

Amounts Paid for Court Expenses, Dec. 10, 1892, to Sept. 3, 1895.

Farmers' Loan & Trust Co.	3,690	96
M. F. Mott.	9,000	00
602 C. Dart, master commissioner	1,000	00
Turner, McClure & Ralston.	9,000	00
		<hr/>
W. L. Prather, special master.	22,690	96
J. G. Winter, " "	500	00
J. G. Winter, " "	3,850	00
W. L. Prather, " "	150	00
" " " "	500	00
" " " "	750	00
Stenographer to " "	85	00
W. L. Prather, " "	1,000	00
Brooks & Wallace, printing court record.	22	00
C. Dart, clerk, court costs.	33	75
" " " "	2,698	48
Brooks & Wallace, printing court record.	149	75
Clarke & Courts, " " " "	732	75
E. H. Graham, all'ce as gen'l att'y	3,900	00
Alfred Abeel, all'ce as receiver.	14,850	00
A. P. McCormick, all'ce as gen'l att'y.	629	05
		<hr/>
Total.	852,541	74

Correct :

C. A. RICHARDSON.

Sheet 3.

Waco & Northwestern railroad—Alfred Abeel, receiver.

Betterments and Additions, Dec. 10, 1892, to Sept'r 3rd, 1895.

Bridges	\$6,253	85
Shops & round-house	1,813	10
Car shed	1,287	80
Water station	50	79
Locomotives	18,140	50
Chair car	6,270	00
Fencing	12,659	36
Total	\$46,505	40

Correct :

C. A. RICHARDSON.

Sheet 4.

603 Waco & Northwestern railroad—Alfred Abeel, receiver.

Land Receipts and Disbursements, Dec. 10, 1892, to Sept. 3, 1895.

Received from Chas. Dillingham, former receiver.....	\$6,383	57
Received from land leases (rents).....	13,935	74
" " " notes.....	14,426	83
" " int. on land notes.....	2,971	49
" " int. on land deposits.....	667	37
Land notes and int. since M'ch 5, 1895, the date of final decree.....	124	23
Total receipts.....	\$38,509	23

Expenses.

Taxes paid.....	\$14,839	97
General land expense.....	1,372	20
	16,212	17
Net land receipts.....	\$22,297	06

Correct:

C. A. RICHARDSON.

Sheet 5.

Waco & Northwestern railroad—Alfred Abeel, receiver.

Earnings and Operating Expenses, Sept. 1 to 3rd, 1895, Inc.

Freight, figured from billing.....	\$1,162	49
Passenger, 1-10 of mo. of Sept.....	474	36
Mail, ".....	48	63
Express, ".....	16	50
Extra baggage, ".....	4	20
Rentals, ".....	31	50
	1,737	68

Expenses.

Maintenance of way & struct., 1-10 of mo. of Sept.....	404	83
" of equipment, 1-10 of mo. of Sept.....	65	66
Conducting transportation, 1-10 of mo. of Sept.....	632	35
General expense, 1-10 of mo. of Sept.....	108	83
	1,211	67
Net earnings for the 3 days.....	\$526	01

Correct:

C. A. RICHARDSON.

Sheet 6.

Indorsements: "Exhibit T I." Waco & Northwestern railroad—Alfred Abeel, receiver. Int. No. 78. Corrected statement of earnings, expenses, &c., from Dec. 10, 1892, to Sept. 3, 1895. Downs. Filed January 6, 1896. C. Dart, clerk, by Geo. H. Burnett, deputy.

Copy of Report of Chas. Dillingham as Receiver W. & N. W. Div., Oct. 1, 1892, to Dec. 10, 1892.

Waco & Northwestern division ac. Chas. Dillingham, receiver H. & T. C. R'y Co.

Earnings.

1892.			
October.	Passenger.....	\$5,412.13	
	Mail.....	357.18	
	Express.....	165.00	
	Freight.....	26,968.05	
	Rental.....	335.00	
		<hr/>	\$83,237.36
Nov'b'r.	Passenger.....	4,647.74	
	Mail.....	357.18	
	Express.....	165.00	
	Freight.....	18,366.66	
	Rental.....	325.00	
		<hr/>	23,861.58
Dec'r 1 to 10, inclusive	Passenger.....	1,904.04	
	Mail.....	115.22	
	Express.....	55.00	
	Freight.....	4,934.85	
	Rental....	108.33	
		<hr/>	7,117.44
			<hr/>
			64,216.38

Expenses.

605	
October:	
Maintenance of way & structures.....	2,982.03
Maintenance of equipment.....	1,543.31
Conducting transportation....	7,305.23
General expenses....	912.52
Stations, warehouses, and stock pens.....	26.13
	<hr/>
	12,769.22
November:	
Maintenance of way & structures.....	3,675.87
Maintenance of equipment.....	1,354.51
Conducting transportation....	9,674.30
General expenses.....	1,083.57
	<hr/>
	15,788.25

Dec. 1 to 10, inc.:

Maintenance of way & structures.....	1,402.61	
Maintenance of equipment.....	442.49	
Conducting transportation.....	14,186.37	
General expenses.....	9,775.81	
	<u>25,807.28</u>	
Less taxes previously charged to this division chargeable to taxes on Downs land and Olcott lands.....	13,790.16	
		<u>12,017.12</u>
Balance to credit W. & N. W. division, Dec. 31, 1892..	40,574.59	
	<u>23,641.79</u>	

Memo.:

Balance to credit as per last statement.....	113,305.44	
Balance to credit as above.....	23,641.79	
	<u>136,947.23</u>	
Less cash paid on Dec. 14, 1892, to A. Abeel, receiver....	100,000 00	
	<u>36,947.23</u>	
Balance to credit Jan. 1, 1893.....		36,947.23

606 Waco & Northwestern div.—ac. Chas. Dillingham, rec'r H. & T. C. R'y.
1893.

Jan. 31. To taxes paid on Downs' lands and not included in previous statements, but chargeable to this division.....	819,098.95	
Feb'y 11. To tax paid on passenger revenue from October 1, 1892, to Dec. 10, 1892....	117.21	
March 15. To cash remitted A. Abeel, re- ceiver.....	17,731.17	
	<u>36,947.33</u>	
CR.		
By balance due W. & N. W. div., as per statement.....	36,947.23	
By cash to balance.....	.10	
	<u>36,947.33</u>	

Indorsements: Int. No. 78. Copy report of Chas. Dillingham, as receiver W. & N. W. div., Oct. 1, 1892, to Dec. 10, 1892. Downs. Filed January 6, 1896. C. Dart, clerk, by Geo. H. Burnett, deputy.

Memorandum of Hearing—Stenographer's Report. Filed Jan'y 6, 1896.

THE FARMERS' LOAN AND TRUST COMPANY, Com-	} No. 227. Eq.
plainant,	
vs.	
THE HOUSTON & TEXAS CENTRAL RAILWAY COM-	
pany <i>et als.</i> , Defendants.	

In re Intervention of Geo. E. Downs, Master. C. No. 69.

Offerings on Behalf of Petitioner in Support of His Petition.

Offered accounts of Receiver Dillingham from April 1, '89, to December 11, 1892, marked "T I to T 4."

The accounts of Receiver Abeel from December 11th, 1892, until September 1st, 1895, marked "T 5 to T 8," being the same receiver's accounts in evidence on the claim of the Lackawanna Coal & Iron Co.

607 Offered in evidence also statement "T Prime" which is a statement prepared by the receiver from his records showing the gross revenues of the Waco & Northwestern Railway Co., the operating expenses, net earnings and other matters called for in the order of reference.

It is understood that the account of the receiver Dillingham for October, November and the first eleven days in December, 1892, will be produced and filed by Mr. Richardson at Waco before the master.

Counsel offered to be produced, if he could do so, a statement from the records of the receiver in 185 and 198 showing the revenues and expenditures of the Waco & Northwestern property between the date of the purchase by Downs, to wit: September 8th, 1888, and April 6th, 1889.

C. A. RICHARDSON, being sworn, testified:

Q. Mr. Richardson, what is your present position?

A. I am receiver's secretary of the Waco & Northwestern railroad.

Q. Have you charge of the records and books of the receivership?

A. They are in the auditor's office: I haven't entire charge, but I work on them.

Q. Are you familiar with them?

A. Yes, sir.

Q. Examine statement "T."

A. That is a statement from the books showing the earnings and operating expenses from Dec., 1892, to December, 1895.

Q. Where is that statement taken from?

A. The books of the receiver.

Q. Is that a correct statement according to the best of your information?

A. It is correct as far as it goes. There are one or two items of earnings that I think belong to earnings that we could not quite arrive at, that occurred during the first three months of the receiver-

ship, and on the short notice we have had to get up this statement we could not give it definitely. It would not affect the expenses or the betterments or the court expenses, and it will take probably five or six days, work to arrive at those items definitely. The first

608 two months of the operation the books were kept down at Houston, then when we moved to Waco the auditor started a new set of books entirely, beginning on the 1st of February, and on the short notice we had it was a matter of impossibility to get these things together and arrive at a definite understanding as to what they were really. There was a good deal of money sent (?) at one time, money that had accumulated while they were operating from December 10 to February 1st, and some of it, I do not know exactly what it was, and I have not had time to find out.

(Objected to as irrelevant.)

Q. I notice in that connection among the receipts specified land notes and leases. Will you explain to the court what that means?

A. That is money that has been collected from land notes given in part payment of purchase of land that was sold when Mr. Dillingham was receiver, and for interest on those notes and for rent of land that had been leased, and this amount that is shown here as received from land notes and lease, \$15,739.39, is the amount received less the expenses. The taxes have been paid out and other expenses, and this is the net amount that was on hand at that time.

Q. That was all you carried into the account?

A. Yes. I did not put that in as running and operating expenses; it comes under the head of receipts from other sources, and that is the net receipts.

Q. Can you tell what proportion of that \$15,000 is for rents collected?

A. No, sir; I could not tell that, but I have an idea as to how the total amount of collections stand. The total amount that has been collected during Mr. Abeel's receivership from land notes and leases is in the neighborhood of \$32,000 and about \$10,500 is for land rents; for lease money.

It was agreed by counsel that Mr. Richardson might prepare a statement explaining these entries and showing what portion of the land notes and leases were for rent and what portion for the price of land sold, and also state what amount was paid out of those receipts for taxes, said statement to be furnished to the master at Waco by Mr. Richardson.

Counsel admits that under the head of court expenses
609 mentioned in account marked Exhibit "T Prime" the amount paid to the Farmers' Loan & Trust Co. was paid under an order of court on account of expenses and commission; that the amount paid M. F. Mott was on account of his fees as solicitor for the complainant; that the amount paid C. Dart was for an allowance made to him for selling the Waco & Northwestern Railway property as special master commissioner in December, 1892, which sale was set aside; that the amount paid Turner, McClure & Ralston was on account of the fees allowed them by the court as solicitors in

this cause for the complainant, and that the other items of this expense account were as stated in the account under the head of betterments and additions.

Q. Just state to the master explanation of the character of each one of these additions.

A. The first item is bridges, and they were new bridges to replace two that were worn out, made by order of the court. Shops and round-houses were all new. Car shed was new. Water station was \$50.79, and that was included in betterments account. That was not made by order of the court. I think it was the tank at Perry enlarged. Locomotives and two new engines. Chair car was new and fencing is all new.

Q. State whether those additions were all in existence at the date of the sale made last September and sold with the property.

A. Yes, sir; all these items were paid before that time; engine and cars and bridges were all in and shops built and fencing done to this amount at that time.

Q. These improvements were in existence when the sale was made last September, and were sold at that time with the property?

A. Yes, sir.

Mr. CAMPBELL: That the Waco & Northwestern branch was sold separately under the final decree rendered in case No. 198 and purchased on Sept. 8th, 1888, by Geo. E. Downs, intervenor here, he paying therefor \$25,000, which was paid down at the time that the sale was duly reported to the court and was confirmed on December

4th, 1888, and deed thereafter made to him by the master 610-615 commissioner on the 18th day of January, 1889, which we will fill in by data to be furnished by Mr. Grant; that the road on application of complainants in this cause was put in the hands of a separate receiver, Charles Dillingham, on the 6th day of April, 1889.

Approved.

WM. L. PRATHER,
Special Master.

Indorsements: Int. No. 78. No. 227. Equity. Master's No., 69. Geo. E. Downs, intervenor. Mem. of hearing. Stenographer's report. Downs. Filed January 6, 1896. C. Dart, clerk, by Geo. H. Burnett, deputy.

616 *Petition of Intervention of Lackawanna Iron and Coal Co. (Int. No. 4). Filed Nov. 3d, 1891.*

U. S. Circuit Court, Eastern District of Texas, at Galveston.

THE FARMERS' LOAN AND TRUST CO., Com-	}	No. 227. In Equity.
plainant,		
<i>vs.</i>		
THE HOUSTON & TEXAS CENTRAL RAIL-	}	
way Company <i>et al.</i> , Defendants.		

To the honorable the judges of the circuit court of the United States for the fifth judicial circuit and eastern district of Texas, at Galveston :

The petition of the Lackawanna Iron and Coal Company, a corporation organized under the laws of the State of Pennsylvania, and, as such, a citizen of said State, legally domiciled at Scranton therein, respectfully represents :

617 First. That on the 28th day of December, 1882, the 26th day of April, 1883, and October 30th, 1883, under and by virtue of three certain contracts bearing said dates, your petitioner which is engaged in the business of manufacturing Bessemer steel rails, did agree to furnish to the said Houston and Texas Central Railway Company, one of the defendants herein, upon the terms and conditions specifically set forth in said contracts, about twenty thousand tons of steel rails, at the prices severally mentioned ; that it was agreed in said contracts that upon the delivery of each five hundred and sixty tons of said rails, or thereabouts, payments were to be made to your petitioner therefor, in cash, or in notes of said company, payable in six months from the average date of delivery to the maturity of the notes, with interest at the rate of six per cent. per annum, and with the privilege of renewing the said notes before their maturity, for a further term of six months, by giving new notes and paying the interest for the additional six months at the rate of six per cent. per annum.

Second. That copies of said contracts, as also of the statements hereinafter referred to in this petition as statements Nos. 1, 2, 3, 4 and 5, were filed by petitioner as annexes to a petition by it filed in suit No. 185 of the chancery docket of this court, styled *The Southern Development Company vs. The Houston and Texas Central Railway Company et als.*, and that your petitioner craves leave to refer to said contracts and statements, which are now of record in this honorable court in the records of said suit, as part of this petition, in like manner as if herein at length set forth, and that petitioner makes said contracts and statements a part of this petition.

Third. That under the first contract of December 28th, 1882, your petitioner delivered about 5,020 tons of rail, and received therefor, under said contract, ten promissory notes of the amounts and dates set forth in said document, marked statement No. 1, of record in said suit No. 185.

Fourth. That under the second contract, of date April 26th, 1883, your petitioner delivered about 5,009 tons of rail, and received therefor promissory notes of the amounts and dates set forth in said document so filed in said record No. 185, and marked statement No. 2.

618 Fifth. That under the third contract, for ten thousand tons, of date October 30th, 1883, your petitioner delivered about eight thousand five hundred and fifty-two tons and received therefor, as detailed in said document on file in said record No. 185, marked statement No. 3, seventeen promissory notes, all dated Houston, Texas, payable to the order of your petitioner, as follows, to wit:

One dated Feb.	21st, 1884,	payable 12 mo. after date.	..	\$20,595	97
"	"	23rd "	"	..	31,439 72
"	"	25th "	"	..	17,130 88
"	"	27th "	"	..	9,233 27
"	March	12th "	"	..	17,526 71
"	"	14th "	"	..	32,281 25
"	"	19th "	"	..	21,154 37
"	"	22d "	"	..	13,791 17
"	April	2d "	six	..	25,294 58
"	"	15th "	"	..	15,478 14
"	"	17th "	"	..	20,121 62
"	"	18th "	"	..	17,888 47
"	"	22d "	"	..	22,539 95
"	May	2d "	"	..	3,788 81
"	"	5th "	"	..	18,936 19
"	"	10th "	"	..	19,480 11
"	"	15th "	"	..	20,494 29

That all of said last-mentioned notes given under said third contract, due six months after date, were, at their respective maturities, as provided in said contract, extended for six months longer, and the interest upon them paid, so that in lieu of the above-mentioned notes, your petitioner received the following:

One note dated Oct. 4, 1884,	payable 6 mo. after date.	..	\$25,294	58
"	" 18 "	"	..	15,478 14
"	" 20 "	"	..	20,121 62
"	" 21 "	"	..	17,888 47
"	" 25 "	"	..	22,539 95
"	Nov. 5 "	"	..	3,788 81
"	" 8 "	"	..	18,966 19
"	" 13 "	"	..	19,480 11
"	" 18 "	"	..	20,494 29

Sixth. That the first five notes given to your petitioner under the first contract of December 28th, 1882, were paid at maturity, and that the other five notes therein mentioned were partially
619 paid at maturity and partially extended, and the extended notes were all finally paid in full.

Seventh. That of the ten notes given to your petitioner under the second contract of April 26th, 1883, some were partially paid at ma-

turity and extended, and the extended notes partially paid and extended further, until your petitioner was left in possession of the following notes as extensions of said original notes, to wit:

One note dated Dec. 24, 1884, payable at 4 months. . . .	\$10,000 00
" " 22, " "	10,000 00
" " 19, " "	10,000 00
" " 31, " "	15,000 00
" Oct. 30, " "	21,000 00
" Sept. 25, " "	20,000 00
" " 20, " "	20,000 00
" Oct. 16, " "	12,000 00

That all of the extensions and renewals of said notes, all the payments of interest thereon, all the payments made of notes at maturity under all of said three contracts, are fully and correctly set forth in the sworn statement, marked statement No. 4, filed in the record of said cause No. 185 of the docket of this honorable court, and referred to as part hereof as hereinabove set forth.

Eighth. That said statements, Nos. 1, 2, and 3, show in detail the exact date of the delivery of each lot of rails under each of said contracts.

That all of the rails under the said first contract were delivered to said defendant in the interval between the 20th of February and the 4th of May, 1883; under the second contract in the interval between the 20th of June and the 21st of September, 1883; and under the third contract, in the interval between February 20th and May 16th, 1884.

That petitioner was proceeding to deliver the balance of said rails under said third contract when they were notified, on or about the 26th day of December, 1884, by the assistant treasurer of said defendant company, that said company would not need the balance of the rails under said contract.

Ninth. That, as appears by the above statement and exhibits, the said Houston and Texas Central Railway Company is indebted unto your petitioner for steel rail furnished as aforesaid in the sum of \$445,175.50, with six per cent. per annum interest thereon, as follows:

On \$20,000 00.	from January 23d, 1885.
" 20,000 00.	" " 28th, "
" 12,000 00.	" February 19th, "
" 20,595 97.	" " 24th, "
" 31,439 72.	" " 26th, "
" 17,130 88.	" " 28th, "
" 9,233 27.	" March 2d, "
" 21,000 00.	" " 2d, "
" 15,000 00.	" " 3d, "
" 17,526 71.	" " 15th, "
" 32,281 25.	" " 17th, "
" 21,154 37.	" " 22d, "
" 13,791 17.	" " 25th, "

"	25,294	58	.....	"	April	7th,	"
"	15,478	14	.....	"	"	21st,	"
"	10,000	00	.....	"	"	22d,	"
"	20,121	62	.....	"	"	23d,	"
"	17,888	47	.....	"	"	24th,	"
"	10,000	00	.....	"	"	25th,	"
"	10,000	00	.....	"	"	27th,	"
"	22,539	95	.....	"	"	28th,	"
"	3,788	81	.....	"	May	8th,	"
"	18,936	19	.....	"	"	11th,	"
"	19,480	11	.....	"	"	16th,	"
"	20,494	29	.....	"	"	21st,	"

That said statement No. 5, hereinabove referred to as part of this petition, contains copies of all the aforesaid twenty-five promissory notes given to your petitioner as aforesaid, all of which are now past due.

Tenth. That all of said steel rails so delivered were used for the useful improvements and necessary repair of the main line of said Houston and Texas Central Railway Co., and of the Western division thereof, and of the Waco and Northwestern division thereof, to the extent hereinafter more fully set forth. That said steel rails were so absolutely necessary to said company to enable it to replace the old iron with which its tracks were laid, that it is doubtful whether said company could have maintained its existence as a common carrier without them. That prior to the improvement and repair of said line of road with steel rails, as aforesaid, accidents to life and limb and damage to property was so great, owing to the condition of the tracks of said company, that the name of the Houston and Texas Central Railway Company became a terror to the traveling and shipping public, and a byword and a reproach. That by means of said steel rails so furnished by petitioner to said defendant railway, the railway of said defendant company has been kept in safe running order, its business and importance increased, and said railway thereby rendered more valuable to the bondholders under the various mortgages thereupon, and especially to the bondholders under the deed of trust and mortgage held by complainant herein, and upon which its bill of foreclosure has been filed in this cause. That said indebtedness was contracted by defendant in consideration of its promise to pay the same out of the earnings of its railway. That your petitioner made the contracts aforesaid and furnished the steel rail aforesaid under the expectation and belief that it would be paid for the same out of the revenues and earnings of said property; and that in case said revenues should not be sufficient, out of the proceeds of the sale thereof, by preference over any of the holders of mortgage bonds secured by deeds of trust on said property, but that said defendant, instead of paying the debt so justly due to your petitioner, out of the earnings of said railway, has entirely failed to pay the same, or any part thereof, as hereinabove set forth, and that the truth is, and your petitioner so charges, that the said defendant has used a large

amount of said earnings for the payment of coupons upon bonds secured by the mortgage upon which a bill of foreclosure has herein been filed, although the holders of said coupons were only entitled to receive payment thereof after the defendant had paid your petitioner the amounts advanced and expended in the manner and for the purposes hereinabove set forth. That said steel rails so purchased by said railway company were actually used for the betterment and improvement of its railway aforesaid, and not for purposes of construction, and that the said rails have been an increment to the value of the property mortgaged to said bondholders, and that your petitioner has the right to claim and does claim that 622 the revenues of said railway property should be applied to the payment of petitioner's said indebtedness, by preference over the claim of any bondholders or coupon-holders, whomsoever.

Eleventh. Your petitioner further alleges that on the 16th day of Feb., 1885, or thereabouts, the Southern Development Company, a body corporate under the laws of the State of California, filed its bill in this honorable court against the said railway company, which said bill is known as No. 185 on the equity docket of this court, wherein the said Southern Development Company set forth the various mortgages and encumbrances upon the railway and other property of said Houston & Texas Central Railway Company, together with various other encumbrances issued by the said defendant railway company. That said Southern Development Company, by its said bill, alleged that said Houston and Texas Central Company was indebted to — in the sum of about six hundred thousand dollars, for money loaned at various times. That said Southern Development Company sought to enforce and effect payment of its said claims, and among other things in said bill, alleged and set forth the embarrassed condition of said railway company, the fact that its various creditors were pressing for payment, and its property was in danger of being scattered, wasted and lost to its creditors, and prayed that this honorable court should take possession of said property by appointment of receivers thereof, and might be pleased to decree that, out of the rents, revenues, issues and profits coming into the hands of said receiver, or receivers, after the payment of all costs, of administration and operating expenses of said railway and necessary expenses for equipment and repair thereto, the claims of said Southern Development Company, together with interest and all cost, might be paid and satisfied.

Twelfth. That said Southern Development Company on its said bill moved this honorable court to appoint receivers of said property, and this honorable court did thereupon, on or about the 21st day of February, 1885, appoint Benjamin G. Clarke and Charles Dillingham as receivers of all the property of said railway company, in the manner and form as set forth in the order appointing said receivers in the record of said suit No. 185.

623 Thirteenth. That said Southern Development Company did thereafter, to wit: on or about the 18th day of April 1885, filed its amendment and supplemental bill, whereby it made Nelson S. Easton and James Rintoul, trustees, and The Farmers'

Loan and Trust Company, trustee, defendants to said bill in their capacities as trustees of various mortgages, upon the property of the defendant company, and that the said Southern Development Company by said amended and supplemental bill further prayed :

1st. That an account might be taken, under the direction of your honors, of the several amounts due to said Southern Development Company by said Houston and Texas Central Railway Company, as also of all sums respectively due to all the other parties creditors of said company who might join said Southern Development Company in the prosecution of said suit, or who might intervene therein for the protection of their claims.

2d. That an account might be taken under the direction of this honorable court as to dates and amounts of money paid by said defendant company to any of the mortgages in the various deeds of trust, or to any holders of the bonds issued under various deeds of trust executed by defendant and secured by the mortgage upon its railways or any portions of the same, and the different times when paid, amounts paid for interest on the said bonds, and on which of the said bonds, as well as all the moneys paid into the sinking fund specified in said mortgages and deeds of trust, and what amounts arising out of the sale of any of the lands or town lots, or other real estate belonging to said railway company, had been paid to said bondholders, or deposited in trust, for their benefit, and that said account might be taken so as to show to this honorable court at what time or times, and what proportion of the said amounts, were paid out of the current revenues of said company, in the absence of any earnings, and what amounts and proportion were so paid out of the net earnings of said defendant railway company.

3d. That an account might be taken of all liens and encumbrances upon said property of said railway company, showing the amount and rank of each and the property affected by each, and also
624 an account of all the assets of every kind and nature belonging to the said railway company.

4th. That for the amounts found due on such accounting to the said Southern Development Company, and all intervening similarly situated persons, there might be a decree against the said railway company and against all of the defendants, declaring that the sums so due were liens upon the net earnings of said railway company, and upon all of its property, superior in rank to the claims of said trustee, and of the mortgage bonds and coupons issued under the said various deeds of trust; that the net earnings of said railway company in the hands of the receivers, appointed in said cause, should be first devoted to the payment of the amounts so decreed, and that if they should not be found sufficient within a reasonable time to pay said amounts, then that a sale of the property and assets of said railway company might be ordered and had in such manner and under such terms and conditions as might be to the best interests of all parties concerned, and that out of the proceeds of said sale, the amounts so due to said Southern Development Company might be first paid in preference to any amounts due on

said mortgage bonds and coupons issued under the various deeds of trust upon the property of said railway company.

5th. And further praying that should the sale of said defendant railway company's property be required to satisfy the decrees of this honorable court, then that said sale should be made in the manner and form as in said bill and supplemental bill set forth.

Fourteenth. That said Clarke and Dillingham, so appointed receivers of the property of said railway company, immediately upon said appointment qualified as receivers, took possession of all the property thereof, entered upon the discharge of their duties as such receivers and continued to act as such until the 10th day of July, 1886, or thereabouts, when they delivered possession of all the property of said railway company then in their possession as also of all revenues of the same which had come into their hands, to Nelson S. Easton and James Rintoul and Charles Dillingham, who had, prior to said 10th day of July, 1886, been appointed joint receivers of said railway company, under the bills of complaint filed by complainants, and upon their application, in the manner and form and under the circumstances set forth in the record of the cause No. 198 of the docket of this honorable court and herein-after more fully set forth.

Fifteenth. Petitioner further avers that said bill and said supplemental bill so filed by said Southern Development Company were by it filed in its own behalf, and in behalf of all other persons similarly situated who might intervene in said suit to protect their own interests, and that petitioner did, by permission of this honorable court, file its petition of intervention in said cause No. 185, on the 12th day of September, 1885, by which petition petitioner prayed that it might be allowed to intervene for its interest and join complainant and become itself a party complainant to said bill against all of the defendants; and whereby petitioner further prayed in all respects as was prayed by complainant, The Southern Development Company, in its bill and supplemental bill of complaint, and further prayed that an account might be taken of the sum due by defendant to petitioner on the contracts hereinabove set forth, and that your honors might decree that the sum found due, with interest, might be ordered to be paid out of the net revenues of the defendant company, and might be declared a lien thereon, and upon all the property of said company, superior in rank to the claims of the trustees, complainants in this bill, and to the mortgage bonds and coupons issued under their various deeds of trust. And whereby your petitioner further prayed for general relief and all such further orders and decrees as might be necessary and proper in the premises.

Sixteenth. That to said bill of said Southern Development Company so filed Nelson S. Easton and James Rintoul, trustees, filed their general and special demurrers, which were by this honorable court sustained, and the whole of said bill and supplemental bill of complaint dismissed with costs on the 27th day of May, 1886, but without prejudice to the rights of complainants to assert their claims, if any they had, in such manner as they might be advised;

and that said receivers, Clarke and Dillingham, were by said decree discharged and ordered to turn over all the property and effects of said railway company, together with all of its accrued revenues in their possession to Nelson S. Easton and James Rintoul and to Charles Dillingham, all of whom had been appointed joint receivers of said railway company in the manner and form as hereinafter set forth, and upon the application of the trustees under the various deeds of trust annexed to the bills of foreclosure in said cause No. 198.

Seventeenth. That prior to the dismissal of said bill in said suit No. 185, said Easton and Rintoul and said Farmers' Loan and Trust Company, had filed three several bills of complaint in foreclosure in this honorable court, against various portions of the railway belonging to said defendant company, and which said bills are known as Nos. 198, 199 and 201 of the chancery docket of this honorable court, and were filed upon the dates following, to wit: the bills in said causes Nos. 198 and 199 on or about the 21st day of January, 1886, and the said bill in said cause No. 201, on or about the 18th day of April, 1886. That prior to the dismissal of said bill in said cause No. 185, this honorable court rendered an order consolidating said three causes, Nos. 198, 199 and 201, and ordering that the said three causes so consolidated should thereafter proceed and be known as "consolidated cause No. 198" of this honorable court, under the title of Nelson S. Easton and James Rintoul, trustees, and The Farmers' Loan and Trust Co., trustee, *vs.* The Houston and Texas Central Railway Company *et als.*, that the complainants in said consolidated cause, prior to the dismissal of said bill in said cause No. 185, had caused the appointment of receivers under their bills in said consolidated cause, to which receivers this honorable court as hereinabove set forth, ordered all the assets of said Houston & Texas Central Railway Company, then in the possession of said receivers, Clarke and Dillingham, to be turned over, as aforesaid, on the 10th day of July, 1886, and that all of the property of said railway company did thereafter remain in the possession of said joint receivers Easton, Rintoul and Dillingham, until the 7th day of December, 1888, or thereabouts, when said Easton and Rintoul were relieved from further duties as such receivers, and said Dillingham has continued as sole receiver in the premises, from said date until the present time.

627 Eighteenth. Petitioner further avers that it is provided by the various deeds of trust securing the mortgage bonds upon the various portions of the railway of the defendant railway company, that the trustees of such mortgages, if they acquire possession of said railway under said mortgages, shall pay any floating debt or debts of said company out of the gross earnings of the said railway, and that, under and by virtue of said provision, your petitioner's claims aforesaid are specially made preferred claims upon the gross earnings of said railway, and enjoy priority over all mortgages bearing upon the same, and are entitled to be paid out of the gross earnings of said railway, before said earnings are applied to the payment of any incumbrances whatsoever upon the same, and tha

your petitioner made the loans hereinabove described, relying upon the said clause in the said mortgages, and in the expectation that the said company would comply with the obligation therein recognized by itself and by its mortgage bondholders and that it would pay your petitioner's said claim before applying any part of its gross earnings to the payment of coupons or other bonded indebtedness. That said company and its bondholders are thus not only by law, but by contract, obligated to apply current earnings to payment of current expenses, and that such claims for current expenses are specially made preferred claims upon the gross earnings of said railway over all claims of bondholders.

Nineteenth. Petitioner further avers that said receivers so appointed in said cause No. 185, did, during their administration of the property of said defendant railway company, receive large revenues from the same, said revenues amounting, as petitioner is informed and believes, to a sum exceeding \$3,500,000. That said receivers did also collect outstanding assets belonging to said company delivered to them when they took possession of said railway and of its property, and which outstanding assets realized an amount in cash of about \$100,000. That large portions of said revenues and of said moneys so collected from outstanding assets of said Houston & Texas Central Railway Company were devoted to the permanent improvement and betterment of the property alleged to be
628 affected by the mortgages in favor of the trustees, complainants herein, thus giving increased value to the same, and that the property of said railway company, thus bettered and improved, was transferred from the receivers so appointed in said cause No. 185 to the receivers appointed in said cause No. 198. That said betterments and said improvements had in great part been made upon said railway by said receivers, prior to the filing of bills of foreclosure by any of the mortgage creditors of the defendant railway company; that is to say, prior to the filing of the bills in said causes Nos. 198, 199, and 201 of the docket of this honorable court, and that the receivers so appointed in said cause No. 185, did upon their discharge, transfer to the receivers in said cause No. 198, a very large sum in cash received by them during their administration. Petitioners aver that had this honorable court not taken possession of the property of said railway company, through its said receivers, said company would have been bound in equity and good conscience to pay out of its earnings the debt due to your petitioner as aforesaid. That this honorable court, in enforcing the rights of complainant herein, if any they have, ought to do what said railway company would itself have been bound in equity and good conscience to do, if it had remained in possession of its property; that is to say, to pay out of its earnings all debts chargeable upon its earnings. That petitioner's debt is one so chargeable, not only upon the funds and earnings of said railway company, which came into the hands of this honorable court at the date of the appointment of receivers in said causes Nos. 185 and 198, but also upon all such funds and earnings as have come into the hands of this honorable court during the pendency of said receiverships aforesaid, and that the using of the

earnings of said receiverships in betterments and extraordinary repairs and improvements to said railway has increased the security of the bondholders of said company at the expense of its supply creditors, and constituted such a use of the current debt fund for the benefit of said bondholders as to render it equitable and proper that the income of said receiverships, accrued and to accrue, should be henceforth used in the way in which said company would have been bound in equity and good conscience to use the same if no change in the possession of

629 said railway company had occurred; that is to say, to pay all debts chargeable upon its earnings, and that if the income of said receiverships now in the possession of this honorable court, or hereafter to accrue, be insufficient to pay the debts due to your petitioner and other persons similarly situated, then said debts should be paid by reimbursing a sufficient amount for said purpose to the current debt fund for the proceeds of any sales of the property of the defendant railway company, to be made herein under the decree of this honorable court, and that your honors should make provision in any decree herein to restore to the current debt fund, and distribute between your petitioner and other persons similarly situated such an amount as may, upon a full and fair accounting, appear to have been applied by said railway company prior to said receiverships or by this honorable court pending said receiverships, from the current debt fund to the payment of interest or fixed charges upon said railway, or to the making of betterments and extraordinary repairs upon the same.

Twentieth. Petitioner further avers that, at the date when the first of said foreclosure bills was filed, to wit, on the 28th day of January, 1886, said receivers, in said cause No. 185, had in their possession free from any encumbrance in favor of any bond or coupon holders of said railway company, a sum of \$350,000, or thereabouts, in cash, and had, prior to said date, as petitioner is informed and believes and alleges, expended a sum of \$70,000 for new locomotives, \$225,000, or thereabouts, for new steel rails, and made other expensive repairs and betterments all in the manner and form as set forth in the report of said receivers, made to this honorable court on the 28th day of February, 1886, on file in this honorable court in the record of said suit No. 198, and which petitioner prays leave to refer to as part hereof.

Petitioner avers that in and to said sum of cash in the hands of said receivers, at the date of the filing of said foreclosure bill, said trustees, complainants herein, and the bondholders and coupon-holders of said railway company are without any right, title, interest or lien, either legal or equitable.

630 Twenty-first. Petitioner further avers that the receivers in said cause No. 198 did receive from the receivers in said cause No. 185 a large sum in cash, which petitioner, upon information and belief, avers to have amounted to about \$140,000, and that said receivers did also receive a large quantity of material from said receivers in said cause No. 185, and a large amount of assets of said Houston and Texas Central Railway Company, all as

per inventory on file in said cause No. 198, and that said receiver Dillingham is continuing to make extensive repairs and betterments upon said railway, and to administer the same in like manner as the same was administered by the receivers in said cause No. 185. That, while such repairs and betterments are and were undoubtedly necessary in order to put and keep the road in a condition in which it can be safely and advantageously operated, the expenditure occasioned thereby has resulted, and is resulting, in a large diminution of the amount of the current debt fund of the road, which diminution should be equitably compensated and made good by your honors in this case.

Twenty-second. That the receivers in said cause No. 185, and in this cause, have realized the sum of \$150,000, or thereabouts, from the sale of old rails belonging to said defendant railway company, and the whole or a greater portion of which old rails were removed from the tracks of said railway company at points where they have been replaced by said new steel rails sold by petitioner to said railway company, for which new steel rails the debt hereinabove set forth as due from said railway company to petitioner was incurred, and that said railway company was in equity and good conscience, bound to devote the proceeds of said old rails thus replaced by the new rails sold by petitioner to said railway company to the payment of the indebtedness due by said railroad company to your petitioner for said new rails, and that this honorable court should appropriate the proceeds of said old rails to the same purposes to which they should have been devoted by said railway company had this honorable court not taken possession of the assets of said railway company. Petitioner further refers to the records of said suits Nos. 185 and 198 as part of this petition in like manner as if the same were herein at length transcribed.

631 Twenty-third. That upon the petition of your petitioner so filed in said cause No. 198, a report was duly filed by the Honorable John G. Winter, special master in said cause, finding that under the facts of the case the debt for which petitioner filed its petition in said cause was of a character equitably entitling it to be discharged in preference to the debts embraced in the mortgages represented in said suit but which preference should be applicable to so much only of petitioner's debt as would remain unsatisfied after exhausting one hundred and seventy (170) certain bonds pledged as security, as recited in the report of the master in said cause, and recommending that a decree be entered accordingly; all of which, with other necessary particulars, will more fully appear from the report of said special master in said cause No. 198, to which report reference is made as part hereof, in like manner as if the same were herein at length transcribed; that complainant in this cause is and was a party to said cause No. 196, and did file exceptions to the report of said special master so filed upon the petition of your petitioner, but that said complainant herein has never brought said exceptions to a hearing, and that the same are still pending in this honorable court in said cause No. 198.

Twenty-fourth. That your petitioner is informed and believes, and

so avers that a large portion of the steel rails so furnished by petitioner to said defendant railway company were for the use and benefit of and were actually used upon and now constitute part of the railway described in the bill of complaint in this cause. That by orders heretofore rendered by your honors in this cause, the receivership so existing in said cause No. 198 has been extended to this cause, and that your petitioner in order more fully to protect its rights in the premises, and in order to obtain a decree by this honorable court as to the proportion of its claim chargeable upon the railways upon which a foreclosure is sought in this cause, desires to intervene therein for its interests.

Twenty-fifth. That your petitioner did during the year 1889, file suit upon its said claim in the district court of Dallas county, a court in the State of Texas of competent jurisdiction in the premises, and did in said suit obtain a judgment against said railway company for the full sum of five hundred and fifty-five thousand 632 nine hundred and fourteen $\frac{25}{100}$ dollars (\$555,914.25), with interest at the rate of eight per cent. per annum from the date of said judgment, the — day of May, 1889, until paid, and that said judgment, under the laws of the State of Texas, constitutes a statutory lien upon the earnings of said railway, whilst in the hands of said receivers, enjoying priority over the claims of any mortgage creditor.

Wherefore, in consideration of the premises, and your petitioner being without adequate relief, except upon the orders of your honors in this cause, prays that your honors will allow this petition to be filed, allow petitioner to intervene herein for its interests, and your petitioner further prays:

1st. That an account may be taken under the direction of your honors of the several amounts due to your petitioner by said Houston and Texas Central Railway Company, together with dates when same became due, and as the same have been liquidated and fixed by said judgment aforesaid.

2nd. That an account be also taken, under the direction of this honorable court, as to the dates and the amounts of money paid by the said defendant railway company to any of the mortgagees in the various trust deeds heretofore described, or described in the record of said cause No. 198, or to any holders of the bonds issued under said deeds of trust, and which bear or bore in whole or in part upon the railways described in the bill of complaint herein; that said account may also state the different times when said amounts were paid, the amounts paid for interest on said bonds, and on which said bonds, as well as all moneys paid into the sinking funds specified in said mortgage or deed of trust, and what amounts arising out of the sales of any of the lands, or town lots, or other real estate belonging to the said railway company, have been paid to the said bondholders or deposited in trust for their benefit; that the said account may be taken so as to show to this honorable court at what time or times, and what proportion of the said amounts were paid out of the current revenues of said company, in the absence

633 of any earnings, and what amounts and proportions were so paid out of the net earnings of the said defendant railway company, and particularly so as to show what amounts and proportions were so paid out of the net earnings of those portions of the railways of the defendant railway company described in the bill of complaint in this cause.

3rd. That an account may be taken showing what proportion of the steel rails furnished by petitioner to said defendant railway was used upon the railways described in said bill of complaint aforesaid.

4th. That an account may be taken of all the liens and encumbrances on the said property of the said railway company, showing the amounts and rank of each, and the property affected by each, and also an account of all the assets of every kind and nature belonging to the said railway company.

5th. That an account may also be taken of all the receipts and expenditures made by said receivers in said cause No. 185, in such manner as to show the dates when said expenditures were made and the character of said expenditures, and particularly in such manner as to show which of such expenditures were made for operating and running expenses of said railway, and which of said expenses were made for extraordinary repairs, betterments and improvements of the property of said railway company, and for the payment of fixed charges upon the same.

6th. That for the amounts found due on such accounting to your petitioner and equitably chargeable upon the railways described in the bill of complaint in this cause there be a decree against the defendant railway company, and against all of the parties complainants and defendants herein, declaring that the sums so due are liens upon the net earnings of said railway company, and especially upon those portions of said net earnings which have accrued or may accrue from the railways described in the bill of complaint in this cause, both those accrued prior to said receivership in said cause No. 185, and those accrued and to accrue during the receivership in said cause No. 198, extended to this cause, and upon all of the property of said railway company, superior in rank to the claims of said trustee and of the mortgage bonds and coupons issued under the deed of trust sought to be foreclosed in this cause.

634 7th. That the net earnings of the railway described in the bill of complaint in this cause in the hands of said receiver, accrued or to accrue, be first devoted to the payment of the accounts so decreed, and if they be not sufficient prior to the final decree in this cause to pay said amounts, then that your honors do decree the payment of said amounts out of any proceeds of sale of the property of said railway company to be made under said final decree, the amounts so decreed to your petitioner to be paid in preference to any amount due under the mortgage bonds and coupons issued under the deed of trust annexed to the bill of complaint in this cause.

8th. And your petitioner further prays that this petition stand referred to the special master herein, to take the account hereinabove prayed for, and to investigate and report upon the subject-

matter of this petition with the opinion of the master as to the rank and claim of your petitioner.

And your petitioner prays for such further and general relief in the premises as the case may require, and as to your honors may seem meet and just.

FARRAR, JONAS & KRUTTSCHNITT,

*Solicitors and of Counsel for the
Lackawanna Iron and Coal Co., Petitioner.*

Order.

Let this intervention be filed.

DON A. PARDEE,

Circuit Judge.

October 31, 1891.

Indorsements: "No. 227. (Int. No. 4.) U. S. circuit court, eastern district of Texas, at Galveston. The Farmers' Loan and Trust Co., complainant, *vs.* The Houston & Texas Central Railway Co. *et als.*, defendants. Petition of Lackawanna Iron & Coal Co., and order allowing filing of same. Farrar, Jonas & Kruttschnitt, solicitors for petitioners, Denegre building, Nos. 33 and 35 Carondelet St., New Orleans. Filed Nov'r 3d, 1891. C. Dart, clerk, by W. L. Hanscom, deputy."

635 *Answer of Complainants to Intervention of the Lackawanna Iron and Coal Company (Int. No. 4).*

Circuit Court of the United States.

THE FARMERS' LOAN AND TRUST COMPANY	} No. —.
<i>vs.</i>	
GEORGE E. DOWNS.	

The complainant, The Farmers' Loan and Trust Company, makes these its exceptions, objections and defenses to the petition of intervention of the Lackawanna Iron and Coal Company herein.

I.

The petitioner has not in its said petition made or stated such a case as entitles it in a court of equity to any relief whatever as against the rights of this complainant by virtue of the mortgage sued on in this case, or any rights against that portion of the Houston and Texas Central railway known as the Waco & Northwestern division thereof, which is the subject-matter of this suit, or its property, or any earnings or revenue thereof, in the control of this court, or any remedy in this suit: and the complainant claims all right and benefit of the legal insufficiency of said petition and of all grounds of demurrer thereto, and to the several parts thereof in accordance with the rules of equity, and the practice of this court.

II.

As to the allegations of said petition, respecting the furnishing of rails to the Houston and Texas Central Railway Company, the making of a contract or contracts respecting the same, the delivery of such rails, the receipt of promissory note by the petitioner, the making of any such notes by said railway company, the extension of any such supposed notes, and the payment of any such notes, or of any moneys due on any of them, this complainant is not informed, save by said petitioner, and it leaves the petitioner to make such proof thereof as it be advised, and this complainant claims all benefit of general and special denial thereof, and the right to require strict proof of said intervenor of each and every matter thereof, and the right on its own behalf to produce evidence in controversy of the same.

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III.

And this complainant further answering says, on information and belief, that all indebtedness of every sort and description, which ever existed on the part of said railway company to said petitioner has been fully paid, satisfied and discharged, and that said petitioner has received in full the amount of every claim, note, bond or obligation of any kind and description which it has, or ever has had, against any corporation or any person whatever by reason of any of the matters and things set forth in the petition herein, and this complainant denies each and every allegation therein contained to the contrary thereof.

IV.

As to any allegations in said petition contained respecting the contents of the deed of trust under foreclosure in this suit, under which the complainant is trustee, the complainant prays to refer to the said deed of trust, or to a certified copy thereof, for greater certainty in that behalf, but this complainant expressly denies that by anything in said deed contained the petitioner's pretended claim is specially or in any way made a preferred claim upon the earnings of the Waco & Northwestern division of said railway, and enjoys any priority over said deed of trust, and is entitled to be paid out of the earnings of said railway before said earnings are applied to the payment of coupon interest secured by the deed of trust under foreclosure in this suit, or any other incumbrance upon the same. This complainant is ignorant of the construction of said trust deed claimed to have formed the reliance or expectation under which petitioner made the sale alleged in its petition, and leaves petitioner to its proof on that subject; but it denies that said railway and its bondholders are or ever were in any way obligated to apply current earnings to payment of said claim or any claim or expense before the payment of interest on mortgage bonds, or that such claims are specially made preferred claims upon the gross earnings of said railway over the claims of bondholders, or that said intervenor had any just expectation thereof. And complainant insists that said

alleged expectations, based on default by said railway company and possession or seizure of the property, is wholly inconsistent with any *bona fide* claim as a current earnings creditor of said company.

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V.

And the complainant avers that any improvement to the railroad property subject to the mortgage sought to be foreclosed in this suit, with funds received by the receivers of the Houston and Texas Central Railway Company, instead of the same being paid over to complainant, which may have been effected by the receivers, was effected at the wrongful expense of complainant, and to its detriment as trustee for holders of overdue and unpaid coupons on the bonds secured by the mortgage, to foreclose which this suit is brought and without this complainant's consent, and against its constant and active protest.

If such receivers had not been appointed the company would have been bound in equity and good conscience to pay interest on all its outstanding mortgage bonds in preference to paying any alleged debt to the petitioner, and such is now the duty of the receiver, as complainant is advised. The complainant denies that petitioner's debt is in — way chargeable on any earnings of the railway to the detriment of bondholders, and denies that any betterment, repair or improvement of the railway has increased the security of bondholders at the expense of supply creditors, and constituted such a use of the current debt fund for the benefit of the bondholders as to render it equitable and proper that the income of the receivership should be used to pay all debts chargeable upon earnings; and denies that if the income be insufficient to pay the petitioner and all persons similarly situated then said debts should be paid from the proceeds of sale.

VI.

The complainant admits that in February, 1885, suit was brought against the Houston and Texas Central Railway Company by the Southern Development Company and the road placed in the hands of two receivers, and that the bill in that cause was known as No. 185 on the equity docket, and was dismissed in May, 1886, and the road turned over to three joint receivers, but as to the allegations respecting the petition of the present petitioner in that cause, it refers to the said petition, or a certified copy thereof, for greater certainty.

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VII.

The complainant further alleges that any sums of money that the receivers in said cause No. 185 held at any time in their possession, derived from the Waco and Northwestern division of said Houston and Texas Central railway, were so held for the benefit of the mortgage bondholders, secured by the mortgage foreclosed in this cause with a duty on the part of the receivers, under the direction and advice of the court, to pay out of such income the ordinary and

proper expenses in preserving and operating the said division of said railway committed to their charge, and to pay the balance to the use and benefit of said bondholders.

VIII.

The complainant further avers that in no respect whatever can the claims of the petitioner be considered current expense claims against the railway company or entitled to be paid out of its current income receipts, but the contrary is the case. Complainant is informed, and therefore avers, that at the date of the alleged contracts under which the petitioner claims, the railway was in fair average condition with the roads in Texas, none of which were up to the standard of first-class roads either as to construction or equipment. It was regularly and promptly paying its interest on its bonds, and the bondholders and their trustees had no right to investigate its management, nor were they consulted as to the same. But its stockholding managers conceived a scheme by which they thought to place it in a condition of superiority over other roads in Texas by laying it with steel rails, expecting thereby to be able greatly to increase its business and the value of the stock held by them. This complainant was not informed on the subject, and could have had no voice if informed.

IX.

And this complainant (without admitting the allegations of the petition respecting the agreement or contract between the petitioner and said railway company) says that whatever agreement was made between them contemplated the complete relaying and
639 reconstruction of the entire track and lines of said railway company, including over 516 miles of railway, for a large amount to be paid to said petitioner, and contemplated certain credits, and said petitioner is required to make full and exact proof of the facts relative to said credits and extensions. And complainant is also informed and alleges that a large amount of collateral security was required and taken from said railway company by said petitioner upon said contracts, and it requires full discovery thereof and alleges that said intervenor knew or had full means of knowing, and ordinary prudence required it to know that said railway company was then owing a large amount of other general and floating indebtedness, as shown in the bill of the said Southern Development — in 185, referred to in the intervention, and hereby referred to for its statement thereof. And complainant wholly denies that said intervenor contracted for said indebtedness on the faith or expectation of payment out of the current earnings of said railroad company, or ever was or became a creditor of that class, or entitled to the equities thereof as defined and required in the view of a court of equity in that behalf. That the equitable and substantial and practical owners of a large majority of the stock of said railway company had likewise control of other lines of transportation of great extent, and were parties of large capital and influence, and

that all the said sales by petitioner were upon the future and general credit of said railway company, and upon the reliance on the credit and management of said holders of said stock and the benefits of their patronage and influence, the said intervenor holding intimate and confidential relations with them.

X

The negotiation for said great amount of steel rails was not in the ordinary course of business and dealings, and not with or in reliance upon the corporate officials of said railway company, but originated with and was brought about and dictated by the said managing stockholders of said company. And if, as intervenor in substance and effect alleges, the same was made in anticipation of and looking to the practical insolvency of said railway company and its going into the hands of trustees or receivers before
640 payment for said steel rails, and with a view to supplant and cut out the rights of the mortgage bondholders by priority thus acquired over them, complainant charges that the same was a fraud and conspiracy wholly against equity and good conscience.

The relaying of the said railway with steel rails was not in the exercise of the usual and good faith, power and discretion of the directory of a railroad company for its necessary or customary repairs, but was extraordinary and extravagant, and wholly beyond the authority of the company, with reference to customary good faith repairs, to be paid in the customary manner out of the current earnings of the company.

XI.

The complainant further avers that upon the prayer of said petitioner, The Lackawanna Iron and Coal Company, the latter became and was a co-complainant with the said Southern Development Company in said cause 185, and was prosecuting the same identical claim sued on herein as such co-complainant, and that the said Southern Development Company, on the entry of the decree dismissing its said bill and all the proceedings and claims in said cause, give notice of and was allowed an appeal in said cause to the Supreme Court of the United States from the said decree of this honorable court, and entered into bonds with sureties in the amount fixed by the court to operate as supersedeas to said decree, which bond was duly approved and the said appeal was in all respects perfected, and the said cause No. 185 is now duly appealed to and pending and undetermined in the Supreme Court of the United States.

The intervenor herein is embraced in and a party in said appeal, and complainant submits to the court and pleads that the pendency of said appeal is a bar to the said intervention of the said Lackawanna Company herein, and that the same ought to be dismissed.

XII.

The complainant further avers that if any such indebtedness as is alleged by the petitioner was incurred by said railway
641 company, the same was incurred with full knowledge on the part of the petitioner of the existence of the mortgage,

made to complainant as trustee, to foreclose which this suit is brought, and of the fact that all the property and income of the said railway company included in and belonging to the so-called Waco and Northwestern division of said company was pledged for the payment of the bonds, secured by the mortgage, to foreclose which this suit is brought; and the complainant further alleges that the said division of the railway itself was built and constructed with the proceeds of the sale of the bonds secured by the said mortgage, and that the complainant, as trustee, has in equity and a good conscience a first and paramount claim upon the said division of said railway and property and the earning thereof.

XIII.

The complainant further alleges that about the year 1877 the majority of the stock of the said railway company became the property of one Charles Morgan, who controlled the management of the railway company by means of his ownership of the said stock, and who in the following year caused to be incorporated, by the State of Louisiana, a corporation entitled "Morgan's Louisiana & Texas Railroad and Steamship Company," to which company so incorporated the said Morgan transferred, and thereby vested in it, the ownership of a large majority of the shares of the said railway company. As he was the sole substantial owner of the stock of Morgan's Louisiana & Texas Railroad and Steamship Company, he was able to control and did control the management of the said railway company by means of his ownership of the Morgan Company's stock. Subsequently the ownership of the Morgan Company's stock passed into the hands of certain capitalists, who were the chief owners of certain railway lines running from San Francisco, California, to the Mississippi river, commonly known as the "Southern Pacific system." This ownership of these parties was represented, when said suit No. 185 was brought by The Southern Development Company, complainant therein, a corporation organized under the laws of California for the purpose, among other things, of representing such ownership and control. This complainant has

642 heard rumors to the effect that the stock of said development company has been transferred to some other corporations or corporation, but as to the facts this complainant is not informed; but it expressly avers that however said stock may now be held, the corporation or corporations owning the same are owned and controlled by the same capitalists above mentioned, or their representatives, and in the same interests. Wherefore complainant alleges that the said development company, or whatever corporation may actually hold such stock as aforesaid, is actually the owner (through the Morgan Company) of the majority of the stock of the Houston & Texas Central Railway Company, and that the policy of the latter company and its management is controlled and dictated by the Southern Development Company, and by those who are the owners of its stock. Complainant further alleges that the Houston & Texas Central Railway Company, being controlled as aforesaid,

the parties having such control took measures to have the said railway company thrown into the hands of receivers, as aforesaid, with the object, among other things, of forcing and compelling the owners of bonds, including those for whom this complainant is trustee, to reduce their interest and to settle their claims against the railway company at less than their face. Part of this plan was to set up a large indebtedness on the part of the railway company to the Southern Development Company and the Morgan Company (said companies in fact representing the stockholders of the railway company) and also to other companies, with which the relations, as aforesaid, of their owners were confidential, and to prevent all payment of bonded interest, and to divert all of the earnings of the railway company into a continued, substantial reconstruction thereof, and to claim that the amount of all expenditures therefor were at the expense of the bondholders, and to be deducted from their security and applied to the payment of said floating debts of the company.

The said parties in interest being those who actually owned the majority of the stock of the railway company and controlled its proceedings and policy, proceeded to file in the name of the Southern Development Company said suit No. 185 and obtained
643 the appointment of receivers therein, asking from the court the appointment as receiver of one of the directors and officers of the Lackawanna Iron and Coal Company, intervenor herein, viz : Benjamin G. Clarke, it being desired that he should receive said appointment in the interest of the floating indebtedness and in general furtherance of the scheme above referred to. But this honorable court, on such application being made, refused to appoint said Clarke, except in conjunction with some other person, and thereupon Messrs. Clarke and Dillingham were appointed joint receivers.

The said receivers retained as their counsel and solicitors throughout their receivership the same solicitors who filed and prosecuted the bill No. 185, and the same solicitors proceeded in suit No. 185 to institute the interventions and suits upon the claims of the intervenor herein, and of the Morgan Company, and of the Missouri Pacific Railroad Company, and to claim like priorities for each. And complainant insists that all said parties were alike privy and consenting to, and procuring and responsible for, all the expenditures under said receivership, and that they ought not to be permitted to set up the same as any ground of equity in their behalf against complainant, who has continuously asserted the liability and the said application of the earnings of the said road beyond necessary operating expenses to their said bonded mortgage debt.

XIV.

And the complainant further avers that since the filing of said bills 183 and 184, this complainant and the complainants in said bills have continuously sought to subject the earnings of said railway company to the payment of overdue interest on the mortgage debt, as well as to make good the sinking fund, for which it was bound; and denies all allegations in the interven-

tion seeking to hold it responsible for any other or different application of said earnings or funds, and denies that there are any facts in the course of said receivership in any suit by which, in equity and good conscience, any claim to priority of earnings, or on account of the application thereof, or to the proceeds of old rails sold, or from any other cause, can be set up by the
 644 intervenor as against complainant. The express object and design of said suit 185, as shown therein, was to prevent the trustees from the exercise of their legal rights under the mortgages, from obtaining the possession of the said railroad, and making the application of its earnings and receipts in accordance with the mortgages.

XV.

As to the allegations of the petitioner respecting a petition filed by it in said case No. 198, and a report of the special master thereon in said cause, this complainant prays to refer to the originals thereof on file in this court, for greater certainty in that regard, expressly alleging, however, that this complainant duly filed its exceptions to the said report, to which it also refers as part of this answer, which said exceptions have never been brought on for hearing, and said report has never been confirmed, nor any decision, order or decree rendered by this court on the same.

XVI.

As to whether the petitioner ever filed suit on its said alleged claim, as averred in said petition, and obtained judgment thereon, this complainant is not informed; but it expressly alleges that it was not a party to any such action, and further alleges, being so informed, that said judgment, if obtained, has been paid and satisfied. And it expressly denies being so advised, that any such judgment, if obtained, under the laws of Texas constitutes or ever constituted a statutory lien upon the earnings of the railway whilst in the hands of receivers enjoying priority over the claims of any mortgage creditor.

Wherefore the complainant prays that said petition of the said Lackawanna Iron and Coal Company be dismissed with costs.

THE FARMERS' LOAN & TRUST COMPANY,

By R. G. ROLSTON, *President*.

Attest: E. S. MARSTON, *Sec'y*.

TURNER, McCLURE & ROLSTON,

[SEAL.] M. F. MOTT,

Solicitors for Complainant.

645 STATE OF NEW YORK, }
 Southern District of New York, } ss:

I, Rosewell G. Rolston, being duly sworn, depose and say, that I am president of The Farmers' Loan and Trust Company, the complainant above named, and have been such president for a number

of years past; that I have read the foregoing answer and know the contents thereof, and that the same is true to my own knowledge, except as to those matters therein stated on information and belief, and as to those matters I believe it to be true. That this verification is not made by the complainant because it is a corporation; and that my knowledge is derived from having taken part in the transactions spoken of and from statements made to me and from examination of the papers, and the same constitute my grounds of belief. The seal affixed to said answer is the corporate seal of said complainant, and was so affixed by its authority.

R. G. ROLSTON.

Sworn to before me this 14th day of Nov., 1891.

[SEAL.]

GEORGE C. AUSTIN,
Notary Public, N. Y. Co.

Indorsements: No. 227. Equity. Circuit court of the United States. Int. No. 4. The Farmers' Loan and Trust Company vs. George E. Downs. Answer of complainant to the petition of intervention of the Lackawanna Iron and Coal Company. Turner, McClure & Rolston, attorneys for pl'ff, 22 William street, New York. Filed Dec'r 7th, 1891. C. Dart, clerk.

Petition and Order Allowing Pacific Improving Co. to Join Lackawanna Iron & Coal Co. in Prosecuting Claim.

U. S. Circuit Court, Eastern District of Texas, at Galveston.

THE FARMERS' LOAN AND TRUST CO.

vs.

THE HOUSTON & TEXAS CENTRAL RAILWAY COMPANY
et als.

No. 227.

646 To the honorable the judges of said court:

Your petitioners, The Lackawanna Iron & Coal Company, the original petitioner herein, and The Pacific Improvement Company, a corporation organized under the laws of the State of California, with due respect show:

That during the pendency of the proceedings had by the Lackawanna Iron & Coal Company in the consolidated cause No. 198, styled Nelson S. Easton and James Rintoul, trustees, and The Farmers' Loan and Trust Company, trustee, vs. The Houston and Texas Central Railway Company et als., which are referred to and set forth in the original petition herein, all the rights and claims of said Lackawanna Iron & Coal Company therein set forth were assigned to the other of your petitioners, The Pacific Improvement Company, and since said transfer the said claim has been prosecuted in the name of the—for the account and benefit of the Pacific Improvement Company; and that your petitioner, The Pacific Improvement Company, desires to join in the prosecution of said claim for its own account and benefit.

Wherefore your petitioners pray that this petition may be filed and that an order may be entered herein permitting the Pacific Improvement Company to become a coplaintiff with the Lackawanna Iron & Coal Company in the petition herein filed by said company on Nov. 3d, 1891, and to join the said Lackawanna Iron & Coal Company in the prosecuting of the claim therein set forth for account and benefit of the Pacific Improvement Company; and that notice of this order may be given to the Farmers' Loan & Trust Company and the Houston and Texas Central Railway Company and to George E. Downs.

FARRAR, JONAS & KRUTTSCHNITT,
Counsel & Solicitors.

Order.

Let this petition be filed, and let the Pacific Improvement Company be made coplaintiff with the Lackawanna Coal & Iron Company, in the petition herein filed on Nov. 3rd, 1891, to aid and assist in the prosecuting of said claim, and let the Farmers' Loan and Trust Company, George E. Downs and the Houston and Texas
647 Central Railway Company be notified of this order by service of the same on their solicitors of record.

DON A. PARDEE,
Circuit Judge.

Feb'y 5th, 1892.

Notice of this petition and order accepted for Geo. E. Downs.

WM. GRANT, *Solicitor.*

Feb'y 5, 1892.

Indorsements: No. 227. Int. No. 4. Chancery docket. U. S. circuit court, 5th circuit & eastern district of Texas, at Galveston. Farmers' Loan & Trust Co. *vs.* The Houston & Texas Central R'y Co. *et als.* Supplemental petition of Lackawanna Iron & Coal Co. & Pacific Imp. Co. Filed Feb'y 6th, 1892. C. Dart, clerk, by W. L. Hanscom, deputy. Farrar, Jonas & Kruttschnitt, attorneys for petitioners, Denegre building, Nos. 33 & 35 Carondelet St., New Orleans.

Exceptions, &c., of Moran Bros. and Henry K. McHarg to Int. of Lackawanna Iron and Coal Company.

In U. S. Circuit Court for the Eastern District of Texas, at Galveston.

FARMERS' LOAN & TRUST COMPANY, Trustee,	}	No. 227. Equity.
Complainant,		
<i>vs.</i>		
THE HOUSTON & TEXAS CENTRAL RAILWAY	}	
Company <i>et al.</i> , Defendants.		

The intervenors, Moran Bros. and Henry K. McHarg, make this their exceptions, objections, and defenses to the petition of intervention of the Lackawanna Coal and Iron Company herein:

1. These intervenors adopt the demurrers, pleading and answer of the Farmers' Loan & Trust Company filed herein on December 7, 1891, to the said petition of intervention, and prays that the same be taken and considered as the demurrers, pleading and answer of these intervenors.

2. And in addition thereto these intervenors show that the
648 pretended claim of said intervention accrued more than two years prior to the filing of their said petition of intervention herein, and accrued more than four years prior to the filing of their said petition of intervention herein and as to these intervenors is barred by the statute of limitation of two and four years, which is here specially pleaded.

L. W. CAMPBELL,

Attorney for Intervenors, Moran Bros. and Henry K. McHarg.

Indorsements: "No. 227. Intervention No. 4. Master's No., 68. Lackawanna I. & C. Co. *et al.*, intervenors. Farmers' Loan and Trust Co., trustee, *vs.* H. & T. C. R'y Co. *et al.* Exceptions, &c., of Moran Bros. and Henry K. McHarg. Filed Nov. 16, 1895. Wm. L. Prather, S. M. Filed January 13, 1896. C. Dart, clerk, by Geo. H. Burnett, deputy."

Report of Wm. L. Prather, Special Master, upon the Intervention of the Lackawanna Iron & Coal Co.

Master's No., 68.

In the Circuit Court of the United States for the Eastern District of Texas, at Galveston.

FARMERS' LOAN & TRUST CO., Trustee,
Complainant,
vs.

H. & T. C. R'Y CO. ET AL., Defendants.

No. 227. In Chancery.

Lackawanna Iron & Coal Co., Intervenor.

To the hon. judges of said court:

By authority of an order of the Hon. Don A. Pardee, circuit judge, made October 31st, 1891, the Lackawanna Iron & Coal Co. filed with the clerk of this court at Galveston on November 3rd, 1891, its petition of intervention herein, which petition, by an order of reference entered October 22nd, 1895, at Galveston, by the Hon. A. P. McCormick, circuit judge, and the Hon. D. E. Bryant, district judge, and filed before the special master on November 16th, 1895, was referred to said master "to take the accounts in said petition
649 prayed for, and to investigate and to find and report upon the facts as to the subject-matter of said petition and of the answers thereto;" leave being granted at the same time to the complainant "to amend its pleadings herein before said master in like form and manner as it might on the date of and prior to the above order of reference; and to intervenors, Moran Brothers and

H. K. McHarg, to file such pleadings before said master as they may be advised and in like manner as they might on the date of and prior to the above order of reference; such amendments and pleadings to be filed, however, within thirty days from the date of this order." The master was further ordered to file his report herein on or before the first Monday in January, 1896, said time being extended by order dated January 4th, 1896, to the second Monday in January, 1896.

On November 16th, 1895, the intervenors, Moran Brothers and Henry K. McHarg, filed before me, their answer adopting the "demurrers, pleading and answer of the Farmers' Loan & Trust Company filed herein on December 7th, 1891," to the petition of intervention of the Lackawanna Iron and Coal Company, and pleading also the statutes of limitation of two and four years as a bar to said intervenors' cause of action.

After notice duly extended to all parties in interest, said reference came on to be heard at the U. S. court-room at Galveston, Texas, on December 4th, 1895, when and where appeared E. B. Kruttschnitt, Esqr., solicitor for intervenor, M. F. Mott, Esqr., solicitor for complainant, and L. W. Campbell, Esqr., solicitor for Moran Brothers and Henry K. McHarg.

By consent of all parties, complainant and intervenors, Moran Brothers & Henry K. McHarg amended their answer to the petition of intervention by adding to paragraph 15, of their said answer the following allegation: "But complainant was not party to said cause, or to any cause prior to the filing of the bill herein in its capacity as trustee for the bondholders secured by the mortgage declared on herein."

The issues between the parties being thus made, evidence was heard in part at Galveston, and by agreement of all parties, the hearing was adjourned to Houston, Texas, where on December 5th, 1895, the evidence was further heard, and said hearing further adjourned to Waco, Texas, where on December 23rd, 1895, it was further heard, and said hearing continued from time to time to January 9th, 1896, when the same was concluded.

I file herewith the pleadings of the parties, a list of the evidence introduced, and a memorandum of the hearings at Galveston and Houston.

Upon consideration of the pleadings, the evidence submitted, agreement of counsel and the admissions made by them during the progress of said hearing, I find as follows:

I.

I find that on the 28th day of December, 1882, the Lackawanna Iron & Coal Company entered into a written agreement with the Houston & Texas Central Railway Company, as set forth in a written contract of said date, for the delivery by said Lackawanna Company to said railway company of five thousand tons of Bessemer steel rails, such delivery to be made as nearly as practicable during the months of March, April and May, 1883, and that upon the de-

livery of each five hundred tons, payment should be made therefor in cash, or in the notes of the purchaser, payable at six months from the average date of delivery, with interest from such date at the rate of six per cent. per annum; that 5,020 tons of steel rails were delivered by said Lackawanna Company to said Houston & Texas Central Railway Company, under this contract, at the price of \$40.40 per ton, during the months of February, March, April and May, 1883, in payment for which the railway company executed to the said Lackawanna Company during the said months of March, April and May, ten promissory notes, payable at six months from their respective dates, amounting, with interest, to \$206,932.16, all of which debt was paid by the railway company, either at maturity of said notes or at maturity of other notes given in renewal thereof. A copy of said written agreement is on file as an annex to the petition of intervention of the Lackawanna Iron & Coal Company, in consolidated cause No. 198 of the equity docket of your honorable court, being marked "document A," and a copy thereof is herewith filed and referred to.

651

II.

I find that on the 26th day of April, 1883, the said Lackawanna Company and the defendant railway company entered into another contract in writing, similar in general terms to the contract hereinbefore mentioned—whereby said Lackawanna Company contracted to deliver to said defendant railway company five thousand tons of Bessemer steel rails at \$39.50 per ton, during the month of August, 1883, or earlier, as called for, and that under this contract said Lackawanna Company delivered to said defendant railway company in the months of June, August and September, 1883, 5,009 tons of steel rails, and received in payment therefor ten promissory notes executed by the defendant railway company, dated in 1883, on the days and months following, to wit, June 21st, 22nd, 23rd; August 10th, 14th, 15th; September 6th, 11th, 15th, and 20th; each payable six months after date, and aggregating, with interest, \$201,346.64, it being provided in said contract that the said defendant railway company should have the privilege of renewing such notes before maturity for a further term of six months by paying the interest, six per cent., or adding the interest to the new notes.

I find that said contract was in the words and figures set forth in "document B," annexed to the petition of said Lackawanna Company, filed in said record No. 198, and of which a copy is herewith filed and referred to.

I find that as these notes matured, the payment of so much of the debt as was not satisfied at maturity was extended until in process of such settlements and extensions, the defendant company, in settlement of balance due to said Lackawanna Company under said contract of April 26th, and in satisfaction of all outstanding notes given under that contract, executed and delivered to petitioner eight promissory notes, payable four months from their respective dates,

with six per cent. interest from maturity; said notes being for the amounts, and dates, and identified as follows, to wit:

No. 924 dated Dec. 24, 1884, 4 mos.,	\$10,000.00
" 923 " " 22, 1884, "	10,000.00
" 922 " " 19, 1884, "	10,000.00
" 927 " Oct. 31, 1884, "	15,000.00

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No. 916 " " 30, 1884, "	21,000.00
" 909 " Sept. 25, 1884, "	20,000.00
" 908 " " 20, 1884, "	20,000.00
" 911 " Oct. 16, 1884, "	12,000.00

Total..... \$118,000.00

I find that in the negotiations between the creditor and debtor which resulted in the execution of the renewal notes above described, the creditor—petitioner—demanded that the debtor—the defendant company—should secure such renewal notes by the hypothecation of collaterals; and in response to this demand the defendant company did hypothecate with petitioner, when the renewal notes were delivered, one hundred and seventy bonds, being first-mortgage bonds of the Galveston, Harrisburg and San Antonio Railway Company, of the face value of one hundred and seventy thousand dollars; that is to say, thirty of said bonds were hypothecated to secure the payment of the note for \$20,000.00 dated September 20th; thirty for the note for \$20,000.00 of date September 25th; fifteen for the note of \$12,000.00 of date October 16th; thirty for the note for \$21,000.00 of date October 30th; twenty-five for the note for \$15,000.00 of date October 31st, and forty for the three notes of \$10,000.00 each, of dates December 19th, 22nd and 24th, which several renewal notes are yet unpaid.

I find that the value of said 170 bonds, so loaned, is at present ninety-two and one-half per cent. of the face value thereof, making a total of \$157,250.00. It appears that said bonds are in the possession of the Pacific Improvement Company, assignee of said iron company as collateral as aforesaid, and that no interest on said bonds has been collected by said iron company or by the defendant railway company, but that the same has been collected by said Southern Development Company.

It was agreed by counsel that without making an actual sale of said 170 bonds, the court should consider the same as sold for said amount of \$157,250.00 on December 23rd, 1895, and should apply such sum as a credit as of said date, upon the claim of the Lackawanna Iron and Coal Company, or of the Southern Development Company as the court may determine.

653

III.

I find that on the 30th of October, 1883, the said Lackawanna Company and the said defendant railway company entered into another contract, in writing, being the contract on file as an annex

to the petition of said Lackawanna Company in record No. 198 of the docket of this honorable court, and marked "document C," of which a copy is annexed to and made a part of this finding.

I find that said contract is similar in general terms to those of December, 1882, and April, 1883, and that by it said Lackawanna Company contracted to deliver to the defendant railway company ten thousand tons of Bessemer steel rails at \$36.60 per ton, such delivery to be made as nearly as practicable from February 1st to August 1st, 1884, at the rate of fifteen hundred to two thousand tons per month; that this contract provided that upon the delivery of each five hundred tons of rails, payment should be made therefor, either in cash or in the notes of the defendant railway company, payable at six months from the average date of such delivery, with six per cent. interest added from such date, with the privilege in the purchaser to renew such notes before their maturity for a further term of six months, by paying the interest, or adding the same to such renewals.

I find that under this contract said Lackawanna Company, during the months of February, March, April and May, 1884, delivered to the defendant railway company 8,552 tons of steel rails.

I find that in said March and April, the auditor of the defendant railway company made a statement or "voucher" of rails then delivered under this contract, which statement passed into the hands of the treasurer of the defendant railway company, with a memorandum that notes were to be issued therefor payable at twelve months, and that in pursuance of this memorandum eight notes, payable twelve months from their respective dates, instead of six months, as provided in said contract, were executed by the defendant railway company and sent to said Lackawanna Company, whereupon said Lackawanna Company wrote said defendant railway company, calling attention to the error, but the notes already sent were received as a matter of accommodation to said defendant railway company. That afterwards, in April and

May, 1884, the defendant railway company, in settlement of the balance due upon said 8,552 tons of rails, executed and delivered to said Lackawanna Company nine promissory notes, payable, under the contract, at six months from their respective dates, with the option in the maker of renewal for a like term.

I find that each of these notes were renewed for six months for like amounts as the originals.

I find that said notes were for the amounts and dated as follows, to wit:

No. 826,	dated	February 21,	1884,	12 mos.	.....	\$20,595 97
" 827,	"	"	23,	" " "	.....	31,439 72
" 828,	"	"	25,	" " "	.....	17,130 88
" 829,	"	"	27,	" " "	.....	9,233 27
" 830,	"	March	12,	" " "	.....	17,526 71
" 831,	"	"	14,	" " "	.....	32,281 25
" 832,	"	Mar.	19,	1884, 12 mos.	.....	21,154 37
" 833,	"	"	22,	" " "	.....	13,791 17

" 910, " Oct.	4, " 6 "	25,294 58
" 912, " "	18, " " "	15,478 14
" 913, " "	20, " " "	20,121 62
" 914, " "	21, " " "	17,888 47
" 915, " "	25, " " "	22,539 95
" 918, " Nov.	5, " " "	3,788 81
" 919, " "	8, " " "	18,936 19
" 920, " "	13, " " "	19,480 11
No. 921, dated Nov.	18, 1884, 6 mos.	20,494 29

Total \$327,175 50

IV.

I find that the defendant railway company is indebted to said Lackawanna Company in the amounts of the several notes set forth in the foregoing two statements, the aggregate of the one being \$118,000, and of the other \$327,175.50; total, \$445,175.50, together with interest on the amount of each of said notes at the rate of six per cent. per annum from their respective dates of maturity.

I find that negotiable promissory notes were given petitioner by the defendant company for all rails sold under the three contracts; that all of said sales were made on a stated credit for a fixed period of time, viz: six months after the average date of each delivery, and that said defendant company had the right, under said contracts, to extend the time six months longer from the maturity of said notes; that such extensions were made for the accommodation and to suit the convenience of said defendant company and that said extended negotiable notes remaining unpaid matured as shown above in clauses 2 and 3, during the months of February, March, April and May, 1885.

I find that all the rails delivered under the first contract, and about one-half of the rails delivered under the second contract, were paid for by the railway company prior to the appointment of any receiver of said property, but that the remaining half under the second contract, and all rails furnished under the third contract, are not paid for.

I find that the rails furnished under the second contract were furnished under a contract made a year and ten months prior to the appointment of the receiver in cause No. 185, and about three years and three months prior to the appointment of the receiver in consolidated cause No. 198, and about six years prior to the appointment of the receiver in this cause.

I find that the rails furnished under the third contract were furnished under a contract made about sixteen months prior to the receivership in cause No. 185, and about two years and nine months prior to the receivership in consolidated cause No. 198, and about five years and six months prior to the appointment of the receiver in this cause.

V.

I find that 6.2 miles of the railway of the Waco & Northwestern division of the Houston & Texas Central railway was laid with rails furnished under the first two above-named contracts, but no evidence was submitted to me showing what proportion of said rails was furnished under each of said contracts respectively.

I further find that of 56 pound rails, it requires 88 tons to lay one mile of track.

I find that of the said railway 30.8 miles were laid with rails furnished under the third of the above contracts.

656 I find that it requires 84.86 tons of 54-pound rails to construct one mile of railroad.

I find that the old iron rails removed from the 37 miles of the said Waco & Northwestern division, upon which said steel rails were laid, were received by the receivers in said cause No. 185, and by them sold at the price of \$13.00 per ton, net; that there were 2,960 tons of such old iron rails so removed from said division and so sold; that said rails were sold in the year 1885.

VI.

I find that the debt for which the Lackawanna Company claims payment in its petition herein cannot be classed as a current debt made in the ordinary course of business, as those terms seem generally to be understood, yet it appears that at the time when the contracts hereinbefore mentioned were entered into between said Lackawanna Company and the defendant railway company that the condition of the track of the defendant railway company was such that the demand for new rails upon the most worn portion of the roadway was practically imperative. For a number of years prior to December, 1882, only about 5,000 tons of new rails had been purchased. The road north from Houston for 90 miles was built in 1857, 1861, and thence northward to Denison, 1867-1872. The Western division leading to Austin was constructed in part prior to 1861, and completed in 1873, and the Waco division was completed about 1875. The condition of these roads was bad, except such portions as had been relaid with 5,000 tons of rails purchased prior to December 28th, 1882. There was continual breakage of rails and wrecking of trains, the track was unsafe, and was generally so regarded, not only by "railroad men," but by the traveling public; the damage to merchandise, rolling stock, &c., was continuous, and the need for new rails appears to have been "absolutely necessary as a preservation of human life, the loss of which was liable to occur at any moment."

I find that when the aforesaid contracts were made with the said Lackawanna Company both seller and buyer expected the debts to be paid from the net income of the railway; that the credit
657 extended under said contracts was at the request of and for the accommodation of the defendant railway company and upon its general credit. That said sales were made without any stipulation that security should be given by the defendant company

for said rails, or that payment therefor should be made out of any particular fund or in any particular way; that said sales were for an unusually large amount of rails and the defendant was unable — pay cash therefor, and there was no other way of obtaining said rails except upon credit; and petitioner herein at the time of said contracts and sales had knowledge of the mortgage of June 16th, 1873, given by the defendant railway company upon the properties of its Waco & Northwestern division to secure the first-mortgage bonds, which said mortgage has been herein foreclosed.

I find that the steel rails supplied by said Lackawanna Company under the aforementioned contracts, 18,581 tons were placed in the track of the defendant railway company as soon as received.

VII.

I find that the bonded debt of the defendant railway company, January 1st, 1885, was as follows:

1st mortg. main line, 7 per cent.....	\$6,262,000
“ “ West. div'n.....	2,270,000
“ “ Waco & N. W. div., 7 per cent.....	1,140,000
Consolidated M. L. & West. div., 8 per cent.....	4,118,000
“ Waco & N. W. div., 8 per cent....	84,000
General mortgage 6 per cent....	3,000,000
Income and indemnity.....	500
Total.....	\$16,874,500

VIII.

I find that interest on all classes of the above bonds payable in 1884, amounting to \$1,191,200, was paid as it matured, and that defendant railway company first defaulted in the payment of interest on its bonds January 1st, 1885, when it failed to pay the interest, amounting to \$333,760, due on that date upon its first-mortgage bonds.

658

IX.

I find that the Southern Development Company, a body corporate under the laws of the State of California, did, on or about the 16th day of February, 1885, file its bill of complaint in this honorable court against said defendant company, which said bill is known as No. 185 of the equity docket of your honorable court, wherein said company set forth the various mortgages and encumbrances upon the railway and other property of said defendant company, together with various other encumbrances upon the property of said defendant railway company.

That said company by its said bill alleged that said Houston & Texas Central Railway Company was indebted to it in the sum of about six hundred thousand dollars, for money loaned at various times; that said company sought to enforce and effect payment of its said claims, and, among other things in said bill, alleged and set forth the embarassed condition of said railway company—the fact

that its various creditors were pressing for payment, and its property was in danger of being scattered, wasted and lost to its creditors, and prayed that this honorable court would take possession of said property by appointment of receivers thereof, and might be pleased to decree that out of the rents, revenues, issues and profits coming into the hands of said receiver, or receivers, after the payment of all costs of administration and operating expenses of said railway and necessary expenses for equipment and repair thereto, the claims of said Southern Development Company, together with interest and costs, might be paid and satisfied.

X.

I find that said Southern Development Company, in its said bill, moved this honorable court to appoint receivers of all of the property of said defendant railway company, and this honorable court did, thereupon, on or about the 21st day of February, 1885, appoint Benjamin G. Clarke and Charles Dillingham as receivers of all the property of said railway company, in the manner and form as set forth in the order appointing said receivers in the record of said suit No. 185, and of which order a copy is filed with these findings marked "document D."

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XI.

I find that said Southern Development Company did thereafter, to wit: on or about the 18th day of April, 1885, file its amended and supplemental bill, whereby it made Nelson S. Easton and James Rintoul, and The Farmers' Loan & Trust Company defendants in said bill in their capacities as trustees of the various mortgages upon the property of the defendant railway company, and that said company by said amended and supplemental bill further prayed:

(1.) That an account might be taken under the direction of your honors, of the several amounts due to it by said Houston and Texas Central Railway Company, as also of all sums respectively due to all the other parties, creditors of said company, who might join it in the prosecution of said suit, or who might intervene therein for the protection of their claims.

(2.) That an account might be taken under the directions of this honorable court, as to dates and amounts of money paid by said defendant company to any of the mortgages in said various deeds of trust, or to any holders of the bonds issued under the said deeds of trust, and the different times when paid, amounts paid for interest on the said bonds, and on which of the said bonds, as well as all moneys paid into the sinking fund specified in said mortgages and deeds of trust, and what amounts arising out of the sale of any of the lands, or town lots, or other real estate belonging to said railway company, had been paid to said bondholders or deposited in trust for their benefit, and that said amount might be taken so as to show to this honorable court at what time or times, and what proportion of the said amounts were paid out of the current reve-

dues of said company, in the absence of any earnings, and what amounts and proportion were so paid out of the net earnings of said defendant railway company.

(3.) That an account might be taken of all items and incumbrances upon said property of said railway company, showing the amount and rank of each, and the property affected by each, and also an account of all the assets of every kind and nature belonging to the said railway company.

660 (4.) That for the amounts found due on such accounting to the said Southern Development Company, and all intervening similarly situated persons, there might be a decree against the said railway company and against all the defendants declaring that the sums so due were liens upon the net earnings of said railway company, and upon all of its property, superior in rank to the claims of said trustee, and of the mortgage bonds and coupons issued under the said various deeds of trust; that the net earnings of said railway company, in the hands of the receivers appointed in said cause, should be first devoted to the payment of the amounts so decreed, and that if there should not be found sufficient within a reasonable time, to pay said amounts, then that a sale of the property and assets of said railway company might be ordered and had, in such manner and under such terms and conditions as might be to the best interest of all parties concerned, and that out of the proceeds of said sales the amounts so due to said Southern Development Company might be first paid in preference to any amounts due on said mortgage bonds and coupons issued under the various deeds of trust upon the property of said railway company.

(5.) And further praying that should the sale of said defendant railway company's property be required to satisfy the decree of this honorable court, then that said sales should be made in the manner and form as in said bill and supplemental bill set forth.

XII.

I find that said Clarke & Dillingham, so appointed receivers of the property of said railway company, immediately upon said appointment, qualified as receivers, took possession of the property thereof, entered upon the discharge of their duties as such receivers, and continued to act as such until the 10th day of July, 1886, or thereabouts, when they delivered possession of all the property of said railway company then in their possession, as also of all revenues of the same which then remained in their hands to Nelson S. Easton and James Rintoul and Charles Dillingham, who had prior to said 10th day of July, 1886, been appointed joint receivers of said railway company, under bills of complaint filed by the trustees
661 of certain mortgages upon the main line & Western division of said Houston & Texas Central railway, and also by the Farmers' Loan & Trust Company as trustee of the general mortgage of said Houston & Texas Central Railway Company, and upon their application, in manner and form, and under the circumstances, set forth in the record of cause No. 198 of the docket of this honorable court, and as hereinafter more fully set forth.

XIII.

I find that said bill and said supplemental bill so filed by said Southern Development Company, were by it filed in its own behalf, and in behalf of all other persons similarly situated who might intervene in said suit to protect their own interests, and that said Lackawanna Company did, by permission of this honorable court, file its petition of intervention in said cause No. 185 on or about the 12th day of September, 1885, by which petition it prayed that it might be allowed to intervene for its interest and join complainant and become itself a party complainant to said bill against all of the defendants; and whereby said Lackawanna Company further prayed in all respects as was prayed by complainant, The Southern Development Company, in its bill and supplemental bill of complaint, and further prayed that an account might be taken of the sum due by the defendant to said Lackawanna Company on the contracts hereinabove set forth, and that your honors might decree that the sum found due, with interest, might be ordered to be paid out of the net revenues of the defendant company, and might be declared a lien thereon, and upon all the property of said company, superior in rank to the claims of the trustees, complainants in this bill, and to the mortgage bonds and coupons issued under their various deeds of trust. And whereby said Lackawanna Company further prayed for general relief and all such further orders and decrees as might be necessary and proper in the premises.

XIV.

I find that to said bill of said Southern Development Company, so filed, Nelson S. Easton and James Rintoul, trustees, filed 662 their general and special demurrers, which were by this honorable court sustained, and the whole of said bill and supplemental bill of complaint dismissed, with costs, on the 27th day of May, 1886, but without prejudice to the rights of complainants to assert their claims, if any they had, in such manner as they might be advised; and that said receivers, Clarke and Dillingham, were by said decree discharged and ordered to turn over all the property and effects of said railway company, together with all of its accrued revenues in their possession to Nelson S. Easton and James Rintoul and to Chas. Dillingham, all of whom had been appointed joint receivers of said railway company in the manner and form as hereinafter set forth, and upon the application of the trustees under the various deeds of trust annexed to the bills of foreclosure in said causes Nos. 198, 199 and 201.

XV.

I find that prior to the dismissal of said bill in said suit No. 185, said Easton and Rintoul and complainant herein, as trustees, had filed three several bills of complaint in foreclosure in this honorable court against various portions of the railway belonging to said defendant company, and which said bills are known as Nos. 198, 199 and 201 of the chancery docket of this honorable court, and were

filed upon the dates following, to wit: The bills in said causes Nos. 198 and 199 on or about the 21st day of January, 1886, and said bill in said cause No. 201 on or about the 18th day of April, 1886. That prior to the dismissal of said bill in said cause No. 185, this honorable court rendered an order consolidating said three causes Nos. 198, 199 and 201, and ordering that the said three causes so consolidated, should thereafter proceed and be known as "consolidated cause No. 198" of this honorable court, under the title of Nelson S. Easton and James Rintoul, trustees, and The Farmers Loan and Trust Company, trustee, vs. The Houston and Texas Central Railway Company, *et als.*, and that the complainants in said consolidated cause, prior to the dismissal of said bill in said cause No. 185 had caused the appointment of receivers under their bills in said consolidated cause, to which receivers this honorable court, as hereinabove set forth, ordered all the assets of said Houston and 663 Texas Central Railway Company, in the possession of said receivers, Clarke and Dillingham, to be turned over as aforesaid, on the 10th day of July, 1886, and that all of the property of said railway company remained in the possession of said joint receivers, Easton, Rintoul and Dillingham, until December 7th, 1888, or thereabouts, when said Easton and Rintoul were relieved from further duty and said Dillingham continued as sole receiver in the premises.

The bill so filed by complainant herein as trustee was as trustee under the general mortgage of the Houston and Texas Central Railway Company, a mortgage different from the one forming the subject-matter of the bill of foreclosure herein, which latter is commonly known as the "Waco & Northwestern Division first mortgage."

I further find that the three mortgages declared on in said causes Nos. 198, 199 and 201 were thereafter duly foreclosed, by final decree entered in said consolidated cause No. 198, on the 4th day of May, 1888, and on September 8th, 1888, all the property of said railway company was duly sold under said foreclosure decrees, by a commissioner appointed for that purpose, and at said sale George E. Downs became the purchaser of the Waco & Northwestern division, but his purchase was made subject to the mortgage foreclosed herein, and subject to the right which the court reserved by said decree to charge upon the property or any part thereof the payment of any amount that might be found to be due and payable by reason of intervening petitions theretofore filed in said cause and be entitled to priority over the mortgage debts referred to in said decree, of which said decree a certified copy is herewith filed and referred to.

XVI.

I find that from February 20th, 1885, to the present time, the property of the defendant railway company, forming the subject-matter of the receivership in this cause has continuously been in the possession of this court under proceedings in said suit No. 185, and thereafter in suits Nos. 198 and 227.

I find that no interest has been paid on the bonded indebtedness

by either of the receivers in this cause. I find that Alfred
664 Abeel, receiver in this cause, has expended under the orders
of this court \$46,505.40, for betterments and permanent im-
provements, from December 10th, 1892, to September 3rd, 1895, con-
sisting of bridges, shops and round-house, car shed, water stations,
locomotives, chair car and fencing.

I find that no part of the income arising from the operation of
the road and no part of the proceeds of sales of old rails, old iron,
old cars and engines, which was received by the receivers in causes
Nos. 185 and 198, ever came into the possession of the receiver in
this cause, and the evidence fails to show that any part of the new
equipments purchased by the receivers in causes Nos. 185 and 198,
as shown above, ever came into the possession of the receivers in
this cause. The evidence fails to show that any improvements and
betterments of the property added to the property of the Houston &
Texas Central Railway Company by the receivers in causes Nos. 185
and 198, were made on the Waco & Northwestern division.

I find that prior to April 6th, 1889, no separate accounts were
kept of the receipts and disbursements of the Waco & Northwestern
division, but the same was operated as a branch of the general
system of the Houston & Texas Central Railway Company, and the
evidence fails to show what, if any, of the expenditures made by the
receivers in causes Nos. 185 and 198 for extraordinary repairs, better-
ments and improvements, and for operating and running expenses
were made for said Waco & Northwestern division, and what por-
tion for other divisions of said Houston & Texas Central Railway
Company; and this is true also as to receipts and incomes.

I find that the receivers in cause No. 185 had on hand in cash at
the opening of business on January 21st, 1886, \$175,393.65, but
there is no evidence that any part of said fund came into the pos-
session of the receivers in this cause.

I find that the receiver in cause No. 198 had on hand at the begin-
ning of business on April 6th, 1889, cash amounting to \$215,842.45,
but the evidence does not show that any part of said funds came
into the hands of the receivers in this cause.

XVII.

I find in the mortgage given by the Houston & Texas Cen-
665 tral Railway Company to the Farmers' Loan and Trust Com-
pany, trustee, dated June 16th, 1873, being the same mort-
gage declared on herein, the following provisions:

"And in case the said Houston & Texas Central Railway Com-
pany shall fail, to pay the principal, or any part thereof, or any
installment of the interest, or any part thereof, on any of the said
bonds at any time when the same shall become due and payable
according to the tenor thereof, and for sixty days after having been
demanded, it shall be competent for the said trustee, its successors
or assigns, to enter upon the said railway and the premises and
property herein conveyed, by its attorneys and agents, and take
possession of the same without let or hindrance of the said first

party, and every part and parcel thereof, and the appurtenances, and appoint an agent to operate and manage the same, and receive the revenue and income thereof, applying the said funds after deducting taxes, necessary expenses and counsel fees, to keep the same in good order and repair, and the surplus to pay the principal and interest of all the bonds which may be due and outstanding, and secured hereby *pro rata*, and thereafter, to the payment of any contributions due to the sinking fund herein established. And upon the request of the holders of one-fifth in amount of the bonds so in default which may be at any time outstanding under this deed of trust, it shall be the duty of said second party by its president, or agent duly appointed in its behalf, to enter upon and take actual possession with or without entry or foreclosure of said railway and property herein described, and all and singular each and every part and parcel thereof, and assume its management until the arrears of both principal and interest be paid, or the property sold, as herein prescribed, receiving the rents, revenues and income thereof, and applying them in the same manner as above stated."

"It is however, expressly agreed that the said party of the first part may dispose of the current net revenues and income of all the said property and railway hereby conveyed in such manner as it shall deem best, until default shall be made in the payment of the interest or principal of said bonds, or of any one or more of them, and shall have the right to sell and dispose of any of such real estate or other property as it may own or acquire, which may not be needed or required for the purposes and business of the said Waco & Northwestern division, except in the case of the six thousand acres per mile of completed road, and which sale and conveyance of such outside property shall transfer the said property and title free from encumbrance of this mortgage or deed of trust, and to change its tracks and make any and all alterations necessary for the benefit of the same."

I find that there is no provision in said mortgage, that the trustee may, if it acquired possession of said railway under said mortgage, pay any floating debt or debts of said company out of the gross earnings of said railway.

XVIII.

I find that during the receivership of Clarke & Dillingham, in said cause No. 185, they received from the operation of the railway company, revenues, and expended for operating expenses, taxes &c., the following amounts, to wit:

Amount received from February 23rd, 1885, to January 21st, 1886, two million seven hundred and fifty-eight thousand four hundred and eighty-seven & $\frac{40}{100}$ dollars.....	\$2,758,487.40
Operating expenses, taxes &c., same period.....	2,137,322.44
Balance or surplus.....	<u>\$621,164.96</u>

Amount received from January 21st to July 10th, 1886, one million one hundred and forty-three thousand seven hundred and thirty-one $\frac{5}{100}$ dollars	\$1,143,731.05
For operating expenses, etc., for same period	1,341,753.85
Leaving a deficit for this period of	\$198,022.80
And leaving a net balance from the operation of said railways from February 23rd, 1885, to July 10th, 1886 of	423,142.16

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XIX.

I find that when said Clarke & Dillingham took possession of the property of the defendant railway company, on February 23rd, 1885, they received in cash	\$30,416 34
That they collected assets of the company as follows, to wit:	
Traffic balances and other claims	118,730 08
Sales of old rails on hand February 23, 1885	110,275 00
Sale of old cars	6,500 00
Total	\$265,921 42

XX.

I find that the receivers, Clarke & Dillingham, during the time when they were in possession of said property as receivers and said Easton and Rintoul and Dillingham, while they were in possession as receivers of said property, expended under orders of court the sums following, outside of operating expenses, to wit:

Amount expended in paying liabilities of the defendant railway company	\$23,274 20
Interest paid upon the first-mortgage bonds, of the company, being interest due January 1st, 1885, to July 1st, 1885	751,438 15
Amount expended for new steel rails	245,793 64
Amount expended in payment of certain car-trust notes	125,695 44
Amount expended for new passenger coaches, baggage, mail & express cars, etc., & locomotives ...	265,696 33
Amount expended by said receivers for right of way, fencing track, real estate, depot, round-house, foundry and pattern-house at Houston	126,218 62
Total	\$1,536,116 38
668 I find that of the amount expended, as above. was expended under the receivership of Messrs. Clarke & Dillingham.	384,026 20

The above statement shows receipts and expenditures up to January 9th, 1888, the date when Master Winter heard the evidence on this intervention in cause No. 198, but no proof has been offered before me showing the receipts and disbursements of the receivership in said consolidated cause since said hearing before said master on January 9th, 1888.

XXI.

I find that said Easton & Rintoul and Dillingham during their receivership realized out of proceeds of sale, or collection of old assets of the defendant company, the sum of \$135,889.70.

XXII.

I find that the receivers in cause No. 198 received from the receivers in cause No. 185 the sum of \$138,751.37 in cash.

I find that the receivers in consolidated cause No. 198 after they took possession of the assets of the railway company on July 10th, 1886, and up to the time of the filing of the report of Master Winter, paid liabilities of the receivers, Clarke & Dillingham, taxes, outstanding vouchers, pay-rolls, traffic balances, \$221,421.32, and collected from the amount due said Clarke & Dillingham as receivers in cause No. 185, \$39,016.69.

XXIII.

I find that said Lackawanna Company on November 26th, 1886, filed its petition of intervention in said cause No. 198, praying substantially for the same relief against all the railways, revenues, earnings, moneys, and other properties and assets of the defendant railway company, including those forming the subject-matter of the receivership herein, as is prayed for by its petition of intervention herein against said railways, revenues, earnings, moneys and other properties and assets of said company forming the subject-matter of the receivership in this cause.

669 I find that upon the petition of said Lackawanna Company, so filed in said cause No. 198, a report was duly filed by the Honorable Jno. G. Winter, special master in said cause, finding that under the facts of the case the debt for which said company filed its petition in said cause was of a character equitably entitling it to be discharged in preference to the debt embraced in the mortgages represented in said suit, but which preference should be applicable to so much only of the said company's debt as should remain unsatisfied after exhausting one hundred and seventy certain bonds pledged as security, as was recited in the report of the master in said cause, and recommending that a decree be entered accordingly. Said one hundred and seventy bonds were the same bonds hereinabove fully described under the second paragraph of these findings of facts—that is to say, they were one hundred and seventy-first mortgage five per cent. bonds of the Galveston, Harrisburg and San Antonio railway (Mexican & Pacific extension) of the face value of one thousand dollars each, or of \$170,000 in all. Said master recommended that a decree be entered accordingly.

I find, as above, that The Farmers' Loan and Trust Company, trustee, complainant in said cause No. 198, did file exceptions to the report of said special master, so filed, but that said complainant has never brought said exceptions to a hearing, and that the same are still pending in this honorable court in said cause No. 198.

XXIV.

I find that the said Lackawanna Company did on the 30th day of April, 1889, file suit upon its said claim against the Houston & Texas Central Railway Company in the district court of Dallas county, in the State of Texas, a court of competent jurisdiction in the premises, that citation was issued in said suit May 1, 1889, and served on the 3d day of June, 1889, and judgment was rendered against the said railway company on May 17, 1889, for the full sum of \$555,914.25, being the amount of its claim herein, with interest at six per cent. per annum up to the date of judgment, and that

said judgment further provided that its amount should bear
670 interest at eight per cent. per annum from its date, to wit:

May 17th, 1889, until paid; that execution was issued on said judgment August 19th, 1889, which was returned by the sheriff of Dallas county, Texas, August 20th, 1889, "not executed, there being no property found in Dallas Co. subject to execution."

I find that the notes sued upon had not been renewed or extended and the same are fully described in the certified copy of the record from the district court of Dallas county, Texas, filed with the evidence herewith returned into court and hereby referred to for description.

XXV.

I find that of the interest paid by the receivers on the first-mortgage bonds of the defendant railway company, and hereinabove referred to, the amount of \$79,800.00 consisted in coupons upon the first-mortgage bonds of the defendant company secured by mortgage upon the Waco & Northwestern division of said company, being the property forming the subject-matter of the litigation herein; and I further find that said interest was paid with interest upon the coupons representing the same, which interest aggregated \$11,571.00, making a total amount of interest paid to holders of bonds secured by mortgage on the Waco & Northwestern division of the Houston & Texas Central Railway Company of \$91,371.00, which sum was paid on or about the first day of May, 1887.

These are the interest payments falling due January 1, 1885, and July 1, 1885, and the accrued interest on the coupons representing said interest to the date of payment.

XXVI.

I find that the Pacific Improvement Company, a corporation organized under the laws of the State of California, has during the pendency of the proceedings herein acquired all the rights and claims of the Lackawanna Iron and Coal Company by assignment from said company.

XXVII.

I find that on February 16th, 1895, the Southern Development Company filed its original bill of complaint in cause No. 185, 671 and that the only parties to said bill were the above complainants, and The Houston and Texas Central Railway Company as defendant, and on February 20th, 1885, on said original bill this court appointed Clark & Dillingham receivers of all the property of said railway company.

I find that the complainant in said bill sets forth the various mortgages given by the said railway company upon its main line and branches, and among other mortgages mentioned in said bill is the mortgage, dated June 16th, 1873, given by the Houston & Texas Central Railway Company to the Farmers' Loan & Trust Company on the Waco & Northwestern division, and being the same mortgage declared on herein.

I find that it is alleged in said bill that Easton & Rintoul, trustees in the first mortgage on the main line and the first mortgage on the Western division, and the Farmers' Loan & Trust Company, trustee in the mortgage declared on herein, are all citizens of the State of New York, and that none of said trustees are to be found in this district, and for that reason complainant was unable to make them parties thereto, but prayed the right to make said trustees parties in case they should come within the jurisdiction of the court.

I find that after the appointment of said receivers and on the 20th day of April, A. D. 1885, complainant filed an amended and supplemental bill in said cause No. 185, making Easton & Rintoul, trustees, and The Farmers' Loan & Trust Company, trustee, and Benjamin A. Shephard additional parties defendant, which supplemental bill avers, among other things, that the said Farmers' Loan & Trust Company was trustee in the mortgage declared on herein.

I find that on March 31st, 1885, prior to the filing of said supplemental bill of complaint, the Farmers' Loan & Trust Company filed its petition in said cause No. 185, praying to be made a party thereto, averring, among other things, that it was trustee under several separate mortgages executed by the defendant railway company, and naming among them the mortgage declared on herein. The prayer of said petition was granted, and on April 6th, 1885, this court entered an order in said cause No. 185, allowing the 672 said Farmers' Loan & Trust Company to become a defendant in said suit, and further ordered that it may demur, plead or answer therein on or before the rule day in June, 1885.

I further find that on June 15th, 1885, said Farmers' Loan & Trust Company filed its answer as defendant in said cause No. 185 in answer to the original bill and the supplemental bill of said complainant.

I find that the averments of said answer are all defensive to the said original and amended bill of complaint, and I find that the above are the only pleadings and the only appearance that was made by the said Farmers' Loan & Trust Company in said cause No. 185, and it does not appear from said answer that said Farmers' Loan &

Trust Company, as trustee for any of the mortgages mentioned in said answer, either demanded of the court that said receiver should hold the property from said trustee or in any other manner demand affirmative relief under said mortgages or either of them. That its appearance in said cause No. 185 was simply that of a defendant in opposition to the rights asserted in the original and supplemental bill of complaint.

I find that on October 5th, 1885, Easton and Rintoul, trustees, having become parties defendant to said cause No. 185, filed demurrers to the original and supplemental bills filed therein, and on, to wit, May 27th, 1886, said demurrers came to be heard and were in all things sustained, and the entire original bill and supplemental bill *was* dismissed.

That prior thereto, on, to wit, May 26th, 1886, on motion of the Houston & Texas Central Railway Company to consolidate said causes Nos. 183, 184, 188, 198, 199 and 201, the following order was made:

"Upon consideration thereof it was ordered, adjudged and decreed, and the court doth order, adjudge and decree, as follows, all the parties consenting thereto in open court: That no further proceedings be had in causes Nos. 183, 184 and 188 without notice to the defendant railway company; that causes Nos. 198, 199 and 201, above named, be consolidated under No. 198 under the name and style of Nelson S. Easton and James Rintoul, trustees, and The

673 Farmers' Loan and Trust Company, trustee, against The Houston and Texas Central Railway Company and Benj. A.

Shepard, trustee, consolidated cause; that in said cause Easton & Rintoul shall stand as complainants, as trustees under the mortgages or deeds of trust, made by the defendant railway company, bearing date respectively July 1st, 1886, and December 21st, 1870; that the Farmers' Loan and Trust Company, expressly assenting thereto, shall stand as complainant, as trustee under the mortgages or deeds of trust made by defendant railway company, bearing dates respectively June 16th, 1873, October 1st, 1872, May 1st, 1875, and April 1st, 1881, and that Benj. A. Shepard as defendant, as trustee under the mortgage or deed of trust made by said defendant railway company, bearing date May 7th, 1877; that the bills filed in said causes Nos. 198, 199, and 201 shall stand as bills in said consolidated cause, and may be amended by either complainant as they may be advised by the August rule day, and that any party hereto may file an answer to such original or amended original bills as he may be advised within thirty days after said August rule day."

I find that no other action was taken in said causes Nos. 183, 184, and 188 since the order above mentioned was made, but that consolidated cause No. 198 proceeded to final judgment, and the three mortgages declared on therein were in all things foreclosed, and I find that while the Farmers' Loan and Trust Company, trustee, in the mortgage declared on herein, expressly assented to stand as complainant in consolidated cause No. 198, that it filed no bill of complaint therein.

I find that on 21st day of March, 1887, said Farmers' Loan & Trust Company filed an answer to the petition of Nelson S. Easton and James Rintoul filed the said cause No. 198, wherein and whereby said Farmers' Loan & Trust Company, as trustee under the Waco & Northwestern mortgage prayed the court that any order which should be made in said cause No. 198 directing the payment by the receivers out of the surplus of net earnings in their hands of any coupons falling due under any of the trust deeds by said railway company, might order and provide for payment by the receivers out of the surplus of net earnings in their hands of the two coupons due under the said Waco & Northwestern division trust deed as well as under the said other first mortgage.

674 I find that said application of said Easton & Rintoul, as also an application of the Farmers' Loan & Trust Company, as trustee, for the payment of interest coupons on the bonds secured by first mortgages or deeds of trust, described in the bills of complaint in said consolidated cause came on to be heard on the 27th day of April, 1887, when the order was rendered by this honorable court, that the coupons due January 1st, 1885, and July 1st, 1885, upon said first-mortgage bonds of the Waco & Northwestern division of the Houston & Texas Central Railway Company should be paid with interest upon said coupon due January 1st, 1885, from January 1st, 1885, until May 1st, 1887, at the rate of six per cent. per annum and with interest upon one half of the coupon due July 1st, 1885, from said last-named date until May 1st, 1887, when the same was ordered to be paid, and upon the remaining one-half of said coupon until it should have been paid. I find that said two coupons were pursuant to said order duly paid.

I find that said order expressly declared that it was "without prejudice to the rights of defendant or of any intervenor in this cause, or any final decree to be rendered in the same, nothing herein being decided as to the merits of the claim of the defendants, or of intervenors, and this order not in any manner stopping or affecting the rights of any party or intervenor in this cause."

I find that said Farmers' Loan & Trust Company, as trustee of the first mortgage of the Waco & Northwestern division of the Houston & Texas Central Railway Company, also filed petitions in this honorable court on the 6th day of November, 1888, and on the 20th day of November, 1888, for the payment of the remaining coupon interest due on the first mortgage of the Waco & Northwestern division, upon which said petition no order was ever rendered.

I find that by the final decree rendered in said cause No. 198, on the 4th day of May, 1888, this honorable court expressly reserved the right to charge the property under said decree ordered to be sold with any amounts that it might decree in favor of any interventions then on file, and that the intervention of the said Lackawanna Company was on file at the time of said decree.

675 I further find that the Waco & Northwestern division under the sale in 198 sold for the sum of \$25,000.00, subject to the mortgage declared on herein, which \$25,000.00 was paid in by the purchaser, Geo. E. Downs, to the master commissioner at the

time of his said purchase. That the bondholders secured by the mortgage declared on herein received no part of the proceeds arising from the sale of said road, or any part thereof, under the final decree rendered in said cause No. 198.

I find that subsequently to said decree, to wit, on the 20th day of April, 1889, said Lackawanna Company filed its petition in said cause No. 198, asking that the receivership therein should continue and remain over the property then in the possession of the court, being the property now in the hands of the receiver in this cause, until the claims and demands of said Lackawanna Company upon said property should have been finally decreed upon, and if decreed in its favor should have been finally paid and settled; and further praying the court to render a preliminary order staying the order which had theretofore been rendered directing the delivery of said property to one George E. Downs, who had become the purchaser thereof, and directing the receivers not to deliver the said property to any purchaser until after the final hearing of the matter of said petition.

I find that upon said petition an order was rendered directing the said George E. Downs, and The Farmers' Loan & Trust Company, complainant therein, to show cause why the relief therein prayed for should not be granted; and further directing the receiver to retain possession of said property until the further order of the court; and further ordering that the receivership which had theretofore been ordered in this cause should be concurrent with the original receivership ordered in said cause No. 198, and that the receiver should keep separate accounts of the earnings and expenses of the Waco & Northwestern division of the Houston and Texas Central railway.

XXVIII.

I take the account prayed for in the petition of said Lackawanna Company as follows, to wit:

676 1st. The amounts due to said Lackawanna Company by said Houston & Texas Central Railway Company are the following, to wit:

\$20,000.00.....	Due January	23rd, 1885
20,000.00.....	" "	28th, "
12,000.00.....	" February	19th, "
20,595.97.....	" "	24th, "
31,439.72.....	" "	26th, "
17,130.88.....	" "	28th, "
9,233.27.....	" March	2nd, "
21,000.00.....	" "	2nd, "
15,000.00.....	" "	3rd, "
17,526.71.....	" "	15th, "
32,281.25.....	" "	17th, "
21,154.37.....	" "	22nd, "
13,791.17.....	" "	25th, "
25,294.58.....	" April	7th, "
15,478.14.....	" "	21st, "

10,000.00.....	"	"	22nd,	"
20,121.62... ..	"	"	23rd,	"
17,888.47.....	"	"	24th,	"
10,000.00.....	"	"	25th,	"
10,000.00.....	"	"	27th,	"
22,539.95.....	"	"	28th,	"
3,788.81.....	"	May	8th,	"
18,936.19.....	"	"	11th,	"
19,480.11... ..	"	"	11th,	"
20,494.29... ..	"	"	21st,	"

Or a total of \$445,175.50

I find that said indebtedness has been liquidated by the judgment of said district court of Dallas county at the sum of \$555,914.25, with interest at eight per cent. per annum from May 17th, 1889, until paid.

2nd. I find that during the years 1883 and 1884 the defendant paid \$2,386,400.00 interest upon its bonds, which amount, less \$1,043,198.27, which seems to have been borrowed for interest purposes in those years, was presumably (it not appearing otherwise), paid from its income or current earnings, and that out of said total the sum of \$159,600.00 was paid as interest upon the first *first* mortgage bonds of the Waco & Northwestern division, being the bonds forming the subject-matter of the bill of complaint in this cause. That said amounts were paid at or about the dates when said interest became due; that is to say, \$39,900.00 on or about the 1st day of January, 1883; a like sum on or about the 1st day of July, 1883; a like sum on or about the 1st day of January, 1884, and a like sum on or about the 1st day of July, 1884. That during 1883 and 1884, two and a quarter million dollars approximately was expended from the earnings and general income of the defendant company's property in the payment of interest on bonds and in additional equipments, permanent improvements, etc.

I find the gross earnings, operating expenses and taxes, extraordinary repairs, renewals and equipments, interest on the funded or bonded debt, and other matters relating to the income and expenditures of the defendant railway company during the years 1874 to 1884 inclusive to have been as per table annexed to and made a part of this finding.

	1874.	1875.	1876.	1877.	1878.	1879.	1880.	1881.	1882.	1883.	1884.
Gross earnings.....	2,784,298 76	3,156,396 23	2,902,396 23	1,905,326 41	2,920,396 64	3,205,684 88	3,741,000 37	3,748,855 10	3,156,517 51	3,251,875 89	2,547,847 40
Operating expenses & taxes.....	2,062,541 42	1,935,963 79	1,855,297 26	1,127,512 00	1,752,028 94	1,773,771 27	2,067,223 35	2,141,870 22	1,748,604 36	1,743,771 28	1,578,190 15
Extraordinary repairs, re- newals & equipment.....	199,554 55	146,886 38	193,828 95	34,165 96	36,933 04	43,567 13	181,797 63	1,063,115 91	549,267 90	782,791 12	641,920 38
Total.....	2,192,895 97	2,084,550 08	2,049,036 21	1,161,617 96	1,788,991 98	1,817,278 40	2,180,129 98	3,294,386 13	2,296,112 26	2,529,562 40	2,220,110 53
Interest on floating debt.....	251,771 40	228,070 59	276,118 74	115,153 78	187,275 08	160,064 24	69,656 16	31,939 09	53,858 12	62,304 79	86,130 21
Interest & principal, State debt.....	61,902 17	62,108 29	59,230 87	53,187 70	52,169 79	47,696 56	43,227 62	42,369 36	41,524 29	40,697 95	39,888 10
Total.....	313,272 57	290,208 79	335,352 61	168,341 48	239,384 87	207,770 80	112,283 72	74,308 29	95,382 41	103,002 74	126,018 31
Surplus.....	278,940 22	784,087 36	517,917 41	575,367 07	892,619 79	1,180,735 68	1,439,566 67	469,360 58	763,622 84	622,220 75	201,718 56
Interest on funded debts.....	879,394 43	877,180 69	1,108,863 94	988,165 00	1,068,315 00	1,098,129 09	1,118,200 00	1,140,260 00	1,136,200 00	1,193,200 00	1,193,200 00
Surplus over interest on bonded debt.....	.....	.....	.....	.....	.....	112,585 68	321,365 67	.....	.....	.....	.....
Deficit over interest on bonded debt.....	581,264 21	33,102 24	650,946 53	412,797 93	175,695 21	.....	.....	670,839 42	439,177,16	570,979 25	991,481 44
Floating debt at close of year.....	1,961,915 60	1,750,957 41	2,092,128 38	2,338,813 97	4,094,397 62	2,573,661 01	1,957,060 07	2,211,765 27	2,928,543 68	2,705,973 21	3,584,251 39

680 I further find that the accounts of said railway company were not kept in such a manner as to indicate the exact fund out of which the interest on said first-mortgage bonds of the Waco & Northwestern division were paid or the exact fund out of which the interest upon the bonds of the other divisions was paid, and that no separate account was kept of the net earnings of said Waco & Northwestern division as distinguished from the net earnings of the other divisions of said railway company either prior to or during the receivership thereof until April 20th, 1889, or thereabouts.

I find that during the receivership in said cause No. 198 the receivers expended in the payment of interest upon the bonds of the issue forming the subject-matter of the bill of foreclosure herein the sum \$79,800.00, being the amount of the coupons due upon said bonds January 1st, 1885, and July 1st, 1885, and that interest was paid upon said coupons, so that the total amount paid out by said receivers for interest on said bonds amounted to the sum of \$91,371.00.

3rd. The facts in reference to the other matters of account prayed for in the petition are fully set forth in the previous findings.

Respectfully submitted.

WM. L. PRATHER,
Special Master.

Indorsements: "No. 227. Equity. Intervention No. 4. Master's No., 68. Farmers' Loan & Trust Co. vs. The Houston & Texas Central R'y Co. *et al.* Master's report upon intervention of Lackawanna Iron & Coal Co. Filed January 13, 1896. C. Dart, clerk, by Geo. H. Burnett, deputy."

Decree, February 26, 1896.

FARMERS' LOAN AND TRUST COMPANY, Complain-	}	Eq. No. 227.
ant,		
v.		
HOUSTON AND TEXAS CENTRAL RAILWAY COM-	}	
pany <i>et al.</i>		

681 In the United States Circuit Court for the Eastern District of Texas, at Galveston.

In the Matter of the Intervention of the Lackawanna Iron and Coal Company and the Pacific Improvement Company.

This day this cause coming on to be heard upon the report of the special master, William L. Prather, to whom this intervention was referred by an order of the court herein entered on the 31st day of October, 1891, under which order the said special master was directed to take accounts in said petition prayed for and to investigate and to find and report upon the facts as to the subject-matter of the said petition and the answers thereto, and the matter having been argued by counsel and duly considered by the court, it is ordered,

adjudged and decreed by the court that the report of the said special master, William L. Prather, on this intervention herein filed on the 13th day of January, 1896, be and the same is hereby confirmed.

And this cause coming on further to be heard upon the said intervention and upon the exceptions and answer thereto of the complainant and upon the answer and exceptions of the intervenors, Moran Brothers and Henry K. McHarg, as well upon the pleadings and evidence, and argument being had thereupon, it is further ordered, adjudged and decreed that said intervention of the said Lackawanna Iron & Coal Company and Pacific Improvement Company be and the same is hereby dismissed without prejudice to the right of the said Lackawanna Iron & Coal Company and Pacific Improvement Company, under or by virtue of its intervention in equity cause No. 198, entitled Easton and Rintoul v. Houston & Texas Central Railway Company. And it is further ordered, adjudged and decreed that the intervenor pay all costs of this intervention.

D. E. BRYANT, *Judge*.

Indorsements: "No. 227. Eq. (Int. No. 4.) The Farmers' Loan & Trust Co. vs. The Houston & Texas Central R'y Co. Decree upon petition of Lackawanna Iron & Coal Co. & Pacific Improvement Co. Filed Feb'y 26, 1896. C. Dart, clerk."

682 *Motion and Order on Appeal, Feb'y 26, 1896.*

In the Circuit Court of the United States for the Eastern District of Texas, at Galveston.

FARMERS' LOAN AND TRUST CO., Trustee, }
Complainant, }
vs. }

THE HOUSTON & TEXAS CENTRAL RAIL- } No. 227. In Chancery.
way Company *et al.*, Defendants; Lack- }
awanna Iron & Coal Co. and Pacific }
Improvement Co., Intervenors. }

On motion of E. B. Kruttschnitt, solicitor for the Lackawanna Iron & Coal Company and the Pacific Improvement Company, intervenors in the above-entitled cause, made in open court, and suggesting to the court that there is error to their prejudice in the final decree rendered and entered at the present term of this honorable court dismissing the intervention originally filed in this cause by said Lackawanna Iron & Coal Company, and thereafter joined in by said Pacific Improvement Company, and that your intervenors are desirous of appealing therefrom to the United States circuit court of appeals for the fifth judicial circuit, said appeal to operate as a supersedeas, and that intervenors file herewith an assignment of errors as part hereof:

It is ordered by the court, in open court, that an appeal be, and the same is hereby allowed to said above-named intervenors from the decree dismissing the above described intervention. Said appeal

to be to the United States circuit court of appeals for the fifth judicial circuit, returnable within thirty (30) days from this date, and the bond for said appeal is hereby fixed at the sum of \$1,000 and said appeal shall operate as a supersedeas.

D. E. BRYANT, *Judge*.

683 In the Circuit Court of the United States for the Eastern District of Texas, at Galveston.

FARMERS' LOAN & TRUST CO., Trustee,
Complainant,

vs.

THE HOUSTON & TEXAS CENTRAL RAIL-
way Company *et al.*, Defendants; Lack-
awanna Iron & Coal Co. and Pacific
Improvement Co., Intervenor.

No. 227. In Chancery.

Assignment of Errors Made Part of Motion of Appeal.

Now come The Lackawanna Iron & Coal Company and The Pacific Improvement Company, appellants from the decree dismissing the intervention originally filed in this cause by the Lackawanna Iron & Coal Company, and thereafter joined in by the Pacific Improvement Company, and assign error in the decree herein rendered against them as follows, to wit:

First. The said decree is erroneous in denying the relief herein prayed for by intervenors, and in dismissing the intervention herein.

Second. That the claim of intervenors is one made for materials and supplies necessary to keep the railways forming the subject-matter of the foreclosure herein a going concern from day to day. That a continuance of the running of said railway involved the interests of the public, the traffic of the road, and the continuance of the franchises of the defendant railway company herein, and that said supplies added to the value of the property mortgaged to complainant herein, and the debt incurred for the same was and is entitled to preference both upon the revenues of the railways forming the subject-matter of this cause, and upon the corpus of the same, over the claims of complainant herein, and that this honorable court erred in not so holding, and in not decreeing in favor of intervenors as in their intervention prayed for.

Third. That the income of the railways forming the subject-matter of the bill of foreclosure in this cause, both prior to the filing of complainant's bill of foreclosure herein and subsequent thereto, and both prior to and subsequent to the taking possession of said

684 railways by this honorable court, was used for the payment of interest upon complainant's mortgage and for permanent improvements upon said railways and was diverted for the benefit of complainant herein and of the holders of bonds described in the mortgage forming the subject-matter of the bill of foreclosure herein, and at the expense of the current debt fund, and that intervenors are entitled to a restoration to the extent of such diversion of said

current debt fund, and that this honorable court erred in not decreeing such restoration and in not decreeing in favor of intervenors upon the current debt fund when thus restored.

Fourth. That the debt of intervenors is entitled to a lien upon the revenues of the defendant railway company in the possession of this honorable court, both under the laws of the State of Texas, and under general principles of equity jurisprudence, and that both under said laws and under said jurisprudence intervenors are entitled to a payment of their claim out of said revenues with priority over the claim of complainant herein and that this honorable court erred in not so holding and ordering.

Wherefore intervenors pray the judgment of the circuit court of appeals on these errors, and for a reversal of the decree appealed from, and for a decree in their favor as by them in their intervention prayed for.

FARRAR, JONAS & KRUTTSCHNITT,
*Solicitors for Intervenor, The Lackawanna Iron & Coal
Company and The Pacific Improvement Company.*

Indorsements: "Eq. 227. Int. No. 4. The Farmers' Loan & Trust Co. v. The Houston & Texas Central R'y Co. *et al.* Assignment of errors of Lackawanna Iron & Coal Co. and Pacific Improvement Co. and order allowing appeal. Filed Feb'y 26, 1896. C. Dart, clerk."

Bond on Appeal.

Know all men by these presents that we, The Lackawanna Iron and Coal Company and The Pacific Improvement Company, as principal, and ———, as sureties, are held and firmly bound unto 685 the Farmers' Loan and Trust Company, as trustee; Moran Brothers, Henry K. McHarg, Collis P. Huntington, E. H. R. Green, George E. Downs, Charles Dillingham, as receiver, the Southern Development Company, Morgan's Louisiana & Texas Railroad and Steamship Company, J. D. Knapp, and W. F. Boyle (all hereinafter referred to and designated as "the said obligees") in the full and just sum of one thousand dollars, to be paid to the said obligees, their certain attorneys, executors, administrators, or assigns; to which payment, well and truly to be made, we bind ourselves, our heirs, executors, and administrators, jointly and severally, by these presents.

Sealed with our seals and dated this — day of February, in the year of our Lord one thousand eight hundred and ninety-six.

Whereas, lately at a regular term of the United States circuit court in and for the eastern district of Texas, at Galveston, in a suit depending in said court, between the Farmers' Loan and Trust Company as complainant and George E. Downs and Charles Dillingham, receiver, as defendants, and Moran Brothers, H. K. McHarg, Collis P. Huntington, E. H. R. Green, Lackawanna Iron and Coal Company, Southern Development Company, Morgan's Louisiana & Texas Railroad and Steamship Company, Pacific Improvement Company, J. D. Knapp and W. F. Boyle, as intervenors, a decree was rendered

denying the relief sought by said Lackawanna Iron and Coal Company and Pacific Improvement Company, intervenors, and dismissing their intervention; and the said Lackawanna Iron and Coal Company and Pacific Improvement Company having obtained an order of appeal in open court upon the same day and at the same term at which said decree was rendered to reverse the said decree in the aforesaid suit, and said appeal being to the United States circuit court of appeals for the fifth circuit, to be holden at New Orleans, Louisiana, within thirty days from the date thereof:

Now, the condition of the above obligation is such, that if the said Lackawanna Iron and Coal Company and Pacific Improvement Company shall prosecute their said appeal to effect, and answer
686 all damages and costs if they fail to make their plea good, then the above obligation to be void; else to remain in full force and virtue.

[SEAL.] LACKAWANNA IRON & COAL COMPANY
& PACIFIC IMPROVEMENT COMPANY,

By E. B. KRUTTSCHNITT, *Their Solicitor.*

[SEAL.] SAM. ALLEN.

[SEAL.] WM. D. CLEVELAND.

Approved by—

D. E. BRYANT, *Judge.*

March 2nd, 1896.

Oath to be Taken by Surety.

I, Sam. Allen, do swear that I am worth, in my own right, at least the sum of five thousand dollars, after deducting from my property all that which is exempt by the constitution and laws of the State from forced sale, and after the payment of all my debts of every description, whether individual or security debts, and after satisfying all incumbrances on my property which are known to me; that I reside in Harris county, State of Texas, and have property in said State liable to execution worth five thousand dollars or more.

SAM. ALLEN, *Surety.*

Sworn to and subscribed before me, this the 29th day of February, A. D. 1896.

As witness my hand and official seal.

[SEAL.]

JNO. H. McCLUNG,

Notary Public, Harris County, Texas.

Oath to be Taken by Surety.

I, Wm. D. Cleveland, do swear that I am worth, in my own right, at least the sum of five thousand dollars, after deducting from my property all that which is exempt by the constitution and laws of the State from forced sale, and after the payment of all my debts of every description, whether individual or security debts, and after satisfying all incumbrances on my property which are known to

me; that I reside in Harris county, State of Texas, and 687-824 have property in said State liable to execution worth five thousand dollars or more.

WM. D. CLEVELAND, *Surety*.

Sworn to and subscribed before me this the 29th day February, A. D. 1896.

As witness my hand and official seal.

[SEAL.]

JNO. H. McCLUNG,
Notary Public, Harris County, Texas.

Indorsements: "Int. No. 4. No. 227, equity docket. United States circuit court, eastern district of Texas, at Galveston. Farmers' Loan & Trust Company, as trustee, complainant, *vs.* The Houston & Texas Central Railway Company *et al.*, defendants. Bond on appeal of Lackawanna Iron and Coal Co. & Pacific Improvement Company. Filed this the second day of March, A. D. 1896. C. Dart, clerk, by W. L. Hanscom, deputy."

825-839 In the Circuit Court of the United States for the Eastern District of Texas, at Galveston.

I, C. Dart, clerk of the circuit court of the United States for the eastern district of Texas, in the fifth circuit and district aforesaid, do hereby certify the foregoing to be a true and correct copy of the record, assignments of errors and all proceedings in the interventions of the Lackawanna Iron and Coal Company, the Southern Development Company, the Morgan's Louisiana and Texas Railroad and Steamship Company, the Pacific Improvement Company, Collis P. Huntington, George E. Downs and E. H. R. Green, in cause No. 227 on the chancery docket of said court, entitled The Farmers' Loan and Trust Company, trustee, *vs.* The Houston and Texas Central Railway Company, Charles Dillingham, receiver, and George E. Downs, as the same now appears on file and of record in my office.

To certify which, witness my hand and the seal of said court, at Galveston, in said district, this 30th day of April, A. D. 1896.

[SEAL.]

C. DART,
Clerk U. S. Circuit Court, Eastern District of Texas,
By W. L. HANSCOM, *Deputy.*

840 PROCEEDINGS IN THE UNITED STATES CIRCUIT COURT OF
APPEALS, FIFTH CIRCUIT.

Argument.

November Term, 1896.

TUESDAY, January 5th, 1897.

(Extract from Minutes.)

THE LACKAWANNA IRON & COAL COMPANY ET AL.	} No. 503.
<i>vs.</i>	
THE FARMERS' LOAN & TRUST COMPANY ET AL.	

This cause came on to be heard this day, and after argument by Mr. E. B. Kruttschnitt, for appellants, the further hearing was continued until tomorrow.

Argument and Submission.

November Term, 1896.

WEDNESDAY, January 5th, 1897.

(Extract from Minutes.)

THE LACKAWANNA IRON & COAL COMPANY ET AL.	} No. 503.
<i>vs.</i>	
THE FARMERS' LOAN & TRUST COMPANY ET AL.	

This cause came on to be heard, and was submitted to the court after further argument by Mr. E. B. Kruttschnitt, for appellants, and by Mr. L. W. Campbell, for appellees, Moran Bros. and McHarg.

Decree of Affirmance.

November Term, 1896.

THURSDAY, February 25th, 1897.

(Extract from Minutes.)

THE LACKAWANNA IRON & COAL COMPANY ET AL.	} No. 503.
<i>vs.</i>	
THE FARMERS' LOAN & TRUST COMPANY ET AL.	

This cause came on to be heard on the transcript of the record from the circuit court of the United States for the eastern district of Texas, and was argued by counsel.

841 On consideration whereof, it is now here ordered, adjudged and decreed by this court, that the decree of the said circuit court in this cause be and the same is hereby affirmed, at the costs of the appellants.

Petition for Rehearing.

United States Circuit Court of Appeals, Fifth Circuit.

LACKAWANNA IRON AND COAL COMPANY ET AL., Ap-	}	No. 503.
pellants,		
<i>versus</i>		
FARMERS' LOAN AND TRUST COMPANY ET AL., Ap-		
pellees.		

The petition of The Lackawanna Iron and Coal Company and of The Pacific Improvement Company, appellants in the above-entitled cause, respectfully represents :

That your petitioners pray for a rehearing in said cause, and for grounds of said rehearing assign the following, to wit :

I.

That this honorable court erred in its conclusion that the claim of petitioners is not one of the character repeatedly recognized by the Supreme Court of the United States as a charge in equity on the continuing income of a railway company, as well that which comes into the hands of the court after the receiver is appointed as that before, and that the court further erred in failing to hold that, in so far as this current-expense creditor is concerned, the court should use the income of the receivership in the way in which the company would have been bound in equity and good conscience to use it, if no change in the possession had taken place ; and that the court further erred in failing to hold that, if the income of a railway company has been diverted from the payment of current-income creditors to the payment of mortgage creditors, or to the improvement of the mortgaged property, the current-income fund, to the extent to which it has been depleted, will be restored out of the proceeds of sale of the mortgaged property.

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II.

That this honorable court, in its opinion, has failed to consider the second proposition advanced by petitioners in the brief filed by them prior to the original hearing, at page 24 thereof, and in the oral argument of this cause, to wit, "that the Farmers' Loan and Trust Company, and the beneficiaries under its trust, have never had a lien upon any of the earnings of the Waco and Northwestern division of the Houston and Texas Central Railway Company, and they have no lien upon any such income now in the hands of the court."

That the court erred in not sustaining the foregoing proposition advanced by petitioners, and in not rendering a decree distributing the income now in the hands of the receiver ratably among all creditors of the defendant railway company before the court, in the event that it should fail to maintain the first proposition advanced by petitioners.

III.

That the court, in its opinion, has failed to consider the third proposition advanced by petitioners in the brief filed by them prior to the original hearing, at page 24 of the same, and in the oral argument, to wit: "If neither party has, nor at any time during this litigation had a lien on the income of the railways mortgaged in this case, then the court will proceed upon the principle that equality is equity, and will distribute the income ratably among all the creditors of the defendant railway company before the court."

That the court erred in not maintaining the said proposition, and in not rendering a decree distributing the income now in the hands of the receiver ratably among all creditors of the defendant railway company before the court, in the event that it should fail to maintain the first proposition advanced by petitioners.

843 Wherefore, petitioners pray that your honors will grant a rehearing herein, and permit this cause to be reargued before this honorable court, especially upon the last two propositions hereinbefore propounded; or in the event that this honorable court will not permit oral argument, then that it will grant said rehearing and permit briefs to be filed in support and amplification of the points above made; and petitioners pray for all further and general relief.

E. B. KRUTTSCHNITT,
E. H. FARRAR,
B. F. JONAS,
H. T. GURLEY,

Solicitors and of Counsel for Petitioners, The Lackawanna Iron and Coal Company and The Pacific Improvement Company, Appellants.

I hereby certify that the points presented in the above petition for a rehearing are in my opinion well founded in law.

E. B. KRUTTSCHNITT,
Of Counsel for Petitioners and Appellants.

Endorsed: Filed March 16, 1897. J. M. McKee, clerk.

Order Denying Petition for Rehearing.

United States Circuit Court of Appeals, Fifth Circuit.

November Term, 1896.

THURSDAY, June 10th, 1897.

(Extract from Minutes.)

LACKAWANNA IRON & COAL COMPANY ET AL.	} No. 503.
^{vs.}	
FARMERS' LOAN & TRUST COMPANY ET AL.	

Ordered, that the petition for rehearing filed in this cause be, and the same is, hereby denied.

Filed Feb'y 25, 1897.

United States Circuit Court of Appeals, Fifth Circuit, November Term, 1896.

LACKAWANNA IRON & COAL COMPANY ET AL., Appellants,	} No. 503.
vs.	
FARMERS' LOAN & TRUST COMPANY ET AL., Appellees.	

Appeal from the circuit court of the United States for the eastern district of Texas.

Before Toulmin, Maxey and Parlange, district judges.

Statement.

On February 16, 1885, the Southern Development Co. filed its bill of complaint in the U. S. circuit court for the eastern district of Texas, against the Houston & Texas Central Railway Co. in a cause known as cause No. 185 of the equity docket of that court. The complainant alleged that the railway company was indebted to it in the sum of about \$600,000 for money loaned at various times, and prayed for the appointment of a receiver. On February 21, 1885, receivers were appointed, and they took possession of all the property of the railway company.

On April 18, 1885, the Southern Development Co. filed its supplemental and amended bill in cause No. 185, whereby it made N. S. Easton and James Rintoul and The Farmers' Loan and Trust Co. defendants in their capacities of trustees of the various mortgages on the property of the railway company. The Southern Development Co. further prayed by said supplemental and amended bill, that an account be taken of the several amounts due it by said railway company, as also of all sums due to all the other creditors of said railway company who might intervene for the protection of their claims. An accounting was also asked of all amounts paid by the railway company to any of its mortgagees or bondholders; of all amounts paid for interest on bonds and of other items specified in the pleadings. The Southern Development Co. prayed that the amounts which the accounting would show it to be entitled to be declared liens on the net earnings of the railway company, and upon all its property, superior in rank to the claims of the

845 trustees, and to the mortgage bonds and coupons issued under various deeds of trust executed by said railway company.

On September 12, 1885, the Lackawanna Co. intervened in cause No. 185, and prayed that an account be had of the sum which the railway company owed it on certain contracts to be hereinafter mentioned more fully, and that its claim be decreed to be paid out of the net revenues of the railway company, and declared to be a lien thereon superior in rank to the claim of the trustees and mortgage bonds and coupons.

The bill of complaint of the Southern Development Co. in cause No. 185 was, upon the demurrer of the trustees, dismissed on May 27, 1886, without prejudice to the rights of complainants to assert their rights, if any they had. The decree discharged the receivers in cause No. 185. They were ordered to turn over all the property of the railway company to other receivers who had theretofore, in causes known as equity causes Nos. 198, 199 and 201 of the docket of said court, been appointed joint receivers of the property of the railway company, on the application of the trustees under various deeds of trust bearing on the property. The receivers in cause No. 185 delivered possession of the property to the receivers in causes Nos. 198, 199 and 201, on July 10, 1886.

The three causes, Nos. 198, 199 and 201, were consolidated as "consolidated cause No. 198." In this cause, the Lackawanna Co., on November 26, 1886, filed its intervention praying substantially for the same relief it had prayed for in cause No. 185. A final decree of foreclosure was rendered in cause No. 198, on May 4, 1888, and, on September 8th, 1888, all the property of the railway company was sold, and one, George E. Downs, became the purchaser of the Waco and Northwestern division of the railway company. But his purchase was made subject to the mortgage which was subsequently foreclosed in equity cause No. 227 of the docket of said court, and subject also to the right which the court reserved, to charge upon the property the payment of any amount that might be found due by reason of intervening petitions pending in cause No. 198, and which might be found to be entitled to priority over the mortgage in that cause.

846 The mortgage foreclosed in cause No. 227 is known as the "Waco and Northwestern Division first mortgage," and is a different mortgage from the mortgages upon which the other causes were based. It bore only on the Waco and Northwestern division of the railway company.

On November 3, 1891, the Lackawanna Co., in cause No. 227, filed its intervention which is now before this court. It is substantially the same as the interventions it filed in causes Nos. 185 and 198.

Subsequently to the final decree of May 4, 1888, to wit: on April 20, 1889, the Lackawanna Co. filed its petition in cause No. 198, praying that the receivership therein should continue over the property then in the possession of the court, until its claims should have been finally decreed and paid. On this petition an order was made ordering the receiver to retain possession of the property until the further order of the court. It was also ordered that the receivership, which had theretofore been ordered in cause No. 227, should be concurrent with the receivership in cause No. 198, and that the receiver should keep separate accounts of the earnings and expenses of the Waco and Northwestern division.

On October 21, 1895, Moran Bros. and Henry K. McHarg, holders of bonds secured by the mortgage or deed of trust which is the subject of cause No. 227, intervened in that cause *pro interesse suo*.

The intervention of the Lackawanna Co., in cause No. 227, which is now before this court, alleges that on December 28, 1882, on April

26, 1883, and on October 30, 1883, under three contracts respectively bearing said dates, it is agreed to furnish to the Houston & Texas Central Railway Co. about 20,000 tons of steel rails at prices stated in the contracts, and that upon the delivery of each 560 tons of rails, payments were to be made in cash or in notes of the railway company, payable in six months from the average date of delivery of the rails, with interest at six per cent. with the privilege of renewing the notes before maturity for a further term of six months by giving new notes and paying interest for the additional six months at six per cent. The intervenor alleges that it delivered 5,009

847 tons of rails under the second contract of date April 26, 1883, for which it received the promissory notes of the railway company; and that, under the third contract of date October 30th, 1883, it delivered about 8,552 tons of rails, for which it also received promissory notes of the railway company. The balances now claimed are \$6,426.51 for rails claimed to have been used on the Waco and Northwestern division, under the second contract, and \$99,300.64 for rails claimed to have been used on the same division under the third contract.

Intervenor alleges that the rails which it furnished were employed for the useful improvements and necessary repairs of the main line of the railway company and of its Western division; that the rails were so absolutely necessary to the railway company to replace the old iron with which its tracks were laid, that it is doubtful whether the railway company could have maintained its existence without them, and that prior to the improvement of the railway by means of the rails, accidents to life and limb and damage to property were so great, owing to the condition of the tracks of said company, that the name of the Houston & Texas Central Railway Co. became a terror to the traveling and shipping public, and a byword and a reproach. The intervenor further alleges that by means of the rails furnished by it, the railway has been kept in safe running order, the business increased and the railway rendered more valuable to the bondholders. It is also alleged that the indebtedness was contracted in consideration of the promise of the railway company to pay the same out of its earnings, and that intervenor made the contracts under the expectation and belief that its claim would be paid out of the earnings, by preference over the bondholders.

The intervenor further alleges, "that it is provided by the various deeds of trust securing the mortgage bonds upon the various portions of the railway of the railway company, that the trustees of such mortgages, if they acquire possession of said railway under said mortgages, shall pay any floating debt or debts of said company out of the gross earnings of the said railway, and that, under and by virtue of said provision, your petitioner's claims aforesaid are specially made preferred claims upon the gross earnings of

848 said railway, and enjoy priority over all mortgages bearing upon the same, and are entitled to be paid out of the gross earnings of said railway, before said earnings are applied to the payment of any encumbrances whatsoever upon the same, and that your petitioner made the loans hereinabove described, relying upon

the said clause in the said mortgages, and in the expectation that the said company would comply with the obligation therein recognized by itself and by its mortgage bondholders, and that it would pay your petitioner's said claim before applying any part of its gross earnings to the payment of coupons or other bonded indebtedness. That said company and its bondholders are thus not only by law, but by contract, obligated to apply current earnings to payment of current expenses, and that such claims for current expenses are specially made preferred claims upon the gross earnings of said railway over all claims of bondholders."

It is also alleged that the railway company has not only failed to pay but has used a large amount of the earnings for the payment of coupons on the bonds secured by the mortgage upon which a bill of foreclosure was filed in the cause. Intervenor alleges and claims that the revenues of the railway company should be applied to the payment of the claim for rails by preference over all bondholders and coupon-holders.

By proper pleadings, The Farmers' Loan and Trust Co., complainant in cause No. 227, on December 7, 1891, and Moran Bros. and Henry K. McHarg, intervenors, on January 13, 1896, objected to and opposed the allowance of the demand of the Lackawanna Coal and Iron Co. as a preferential claim. Moran Bros. and Henry K. McHarg specially pleaded the statute of limitation of two and four years.

The matter of the intervention of the Lackawanna Co. was referred to a master, who reported adversely to the demand.

The master's report was not excepted to. *Inter alia*, the master reports the following findings:

On December 28, 1882, intervenor entered into a written contract with the railway company to deliver to it 5,000 tons of steel rails in March, April and May, 1883, payment to be made in cash on delivery of the rails or in notes of the purchaser, payable at six months, with six per cent. annual interest. Under this contract, 5,020 tons of rails were delivered, in payment of which the railway company executed its ten promissory notes to the intervenor, payable at six months, amounting with interest to \$206,932.16; all of which notes were either paid at maturity or at the maturity of other notes given in renewal.

On April 26, 1883, another written contract was entered into by the same parties for the delivery of 5,000 tons of rails during August, 1883, or earlier if called for; payment to be made in cash or in notes of the purchaser payable at six months with six per cent. annual interest. This contract provided that the railway company should have the privilege to renew the notes before their maturity for a further term of six months, by paying the interest, six per cent., or adding the interest to the new notes. Under this contract 5,009 tons of rails were delivered during June, August and September, 1883, and ten promissory notes payable at six months from their dates, dated on divers days in June, August and September, 1883, and aggregating with interest \$201,346.64, were delivered to intervenor. As these notes matured, payment of so much of the

debt as was not satisfied at maturity, was extended, until, in process of such settlement and extension, the railway company, in settlement of the balance due under the contract of April 26, 1883, delivered to intervenor eight promissory notes, payable at four months from their dates, dated on divers days in September, October and December, 1884, and aggregating \$118,000. During the negotiations between intervenor and the railway company, which resulted in the execution of these renewal notes, intervenor demanded that the railway company should secure the renewal notes by the hypothecation of collaterals, and in response to such demand the railway company hypothecated with the intervenor 170 first-mortgage bonds of the Galveston, Harrisburg and San Antonio Railway Co., which, by agreement of counsel, are admitted to be worth \$157,250.

On October 30, 1883, the same parties entered into another written contract, similar in general terms to the other contracts, and containing the clause securing to the railway company the privilege of renewing the notes, and providing for the delivery of 10,000 tons of steel rails between February 1st and August 1st, 1884. Under this contract, intervenor delivered 8,552 tons of rails during February, March, April and May, 1884. Through error, eight notes, in payment of rails supplied under this contract, dated on divers days in February and March, 1884, were made payable at twelve instead of six months. They were, however, accepted by intervenor. Afterwards, in April and May, 1884, the railway company, in settlement of the balance due on the 8,552 tons of rails delivered under the contract of October 30, 1883, delivered to intervenor nine promissory notes, payable at six months from their dates and renewals for a like term at the maker's option. Each of these notes were renewed for six months. The seventeen notes given under this contract were dated on divers days in February, March, October and November, 1884, and aggregate \$327,175.50.

The master's report also contains the following findings:

"I find that negotiable promissory notes were given petitioner by the defendant company for all rails sold under the three contracts; that all of said sales were made on a stated credit for a fixed period of time, viz: six months after the average date of each delivery, and that said defendant company had the right, under said contracts, to extend the time six months longer from the maturity of said notes; that such extensions were made for the accommodation and to suit the convenience of said defendant company, and that said extended negotiable notes remaining unpaid matured, as shown above in clauses 2 and 3, during the months of February, March, April and May, 1885.

"I find that all the rails delivered under the first contract, and about one-half of the rails delivered under the second contract, were paid for by the railway company prior to the appointment of any receiver of said property, but that the remaining half under the second contract, and all rails furnished under the third contract, are not paid for.

851 "I find that the rails furnished under the second contract were furnished under a contract made a year and ten months prior to the appointment of the receiver in cause No. 185, and about three years and three months prior to the appointment of the receiver in consolidated cause No. 198, and about six years prior to the appointment of the receiver in this cause.

"I find that the rails furnished under the third contract were furnished under a contract made about sixteen months prior to the receivership in cause No. 185, and about two years and nine months prior to the receivership in consolidated cause No. 198, and about five years and six months prior to the appointment of the receiver in this cause."

* * * * *

"I find that the debt for which the Lackawanna Company claims payment in its petition herein cannot be classed as a current debt made in the ordinary course of business as those terms seem generally to be understood, yet it appears that at the time when the contracts hereinbefore mentioned were entered into between said Lackawanna Company and the defendant railway company, that the condition of the track of the defendant railway company was such that the demand for new rails upon the most worn portion of the roadway was practically imperative. For a number of years prior to December, 1882, only about 5,000 tons of new rails had been purchased. The road north from Houston for 90 miles was built in 1857-1861, and thence northward to Denison, 1867-1872. The Western division, leading to Austin, was constructed in part prior to 1861 and completed in 1873, and the Waco division was completed about 1875. The condition of these roads was bad, except such portions as had been relaid with 5,000 tons of rails purchased prior to December 28th, 1882. There was continual breakage of rails and wrecking of trains, the track was unsafe, and was generally so regarded, not only by 'railroad men,' but by the traveling public. The damage to merchandise, rolling stock, etc., was continuous, and the need for new rails appears to have been 'absolutely necessary as a preservation of human life, the loss of which was liable to occur at any moment.'"

852 "I find that when the aforesaid contracts were made with the said Lackawanna Company, both seller and buyer expected the debts to be paid from the net income of the railway; that the credit extended under said contracts was at the request of and for the accommodation of the defendant railway company and upon its general credit; that said sales were made without any stipulation that security should be given by the defendant company for said rails, or that payment therefor should be made out of any particular fund or in any particular way; that said sales were for an unusually large amount of rails, and the defendant was unable to pay cash therefor, and there was no other way of obtaining said rails except upon credit; and petitioner herein, at the time of said contracts and sales, had knowledge of the mortgage of June 16th, 1873, given by the defendant railway company upon the properties

of its Waco & Northwestern division to secure the first-mortgage bonds, which said mortgage has been herein foreclosed."

* * * * *

"I find in the mortgage given by the Houston & Texas Central Railway Company to the Farmers' Loan & Trust Company, trustee, dated June 16, 1873, being the same mortgage declared on herein, the following provisions: And 'in case the said Houston & Texas Central Railway Company shall fail to pay the principal, or any part thereof, or any installment of the interest, or any part thereof, or any of the said bonds at any time when the same shall become due and payable according to the tenor thereof, and for sixty days after having been demanded, it shall be competent for the said trustee, its successors or assigns, to enter upon the said railway and the premises and property herein conveyed, by its attorneys and agents, and take possession of the same without let or hindrance of the said first party, and every part and parcel thereof, and the appurtenances, and appoint an agent to operate and manage the same, and receive the revenue and income thereof, applying the said funds, after deducting taxes, necessary expenses and counsel fees, to keep the same in good order and repair, and the surplus to pay the principal and interest of all the bonds which may be due and outstanding, and secured thereby *pro rata*, and thereafter to the payment of any contributions due to the sinking fund herein established.

853 And upon the request of the holders of one-fifth in amount of the bonds so in default which may be at any time outstanding under this deed of trust, it shall be the duty of said second party, by its president, or agent duly appointed in its behalf, to enter upon and take actual possession with or without entry or foreclosure of said railway and property herein described, and all and singular each and every part and parcel thereof, and assume its management until the arrears of both principal and interest be paid, or the property sold, as herein prescribed, receiving the rents, revenues and income thereof, and applying them in the same manner as above stated.' * * *

"It is however expressly agreed that the said party of the first part may dispose of the current net revenues and income of all the said property and railway hereby conveyed in such manner as it shall deem best, until default shall be made in the payment of the interest or principal of said bonds, or of any one or more of them, and shall have the right to sell and dispose of any of such real estate or any other property as it may own or acquire which may not be needed or required for the purposes and business of the said Waco and Northwestern division, except in the case of the six thousand acres per mile of completed road, and which sale and conveyance of such outside property shall transfer the said property and title free from encumbrance of this mortgage or deed of trust, and to change its tracks and make any and all alterations necessary for the benefit of the same."

"I find that there is no provision in said mortgage that the trustee may, if it acquired possession of said railway under said mort-

gage, pay any floating debt or debts of said company out of the gross earnings of said railway."

The lower court confirmed the master's report and dismissed the intervention. The Lackawanna Co. has appealed.

PARLANGE, district judge, delivered the opinion of the court:

It is contended, on behalf of the Lackawanna Iron and Coal Company, that its claim is a preferential one within the doctrine of *Fosdick vs. Schall*, 99 U. S. 225, and other cases in which certain 854 claims were accorded preference over the holders of railroad mortgage bonds. The intervenor's counsel urge that the case of *Burnham vs. Bowen*, 111 U. S. 777, is analogous in principle to the present case. The urgent need of the railway company for the rails supplied by the intervenor, the dilapidated condition of the road prior to the supplying of the rails, the danger to life, limb and property which resulted from such condition, the increased business of the road and the augmented value of the bondholders' security, are asserted and are pressed upon the court's attention as considerations for declaring the intervenor's claim preferential.

Even if all these assertions were sustained by the findings—and some of them do not appear to be so sustained—the intervenor's claim to a preference would, in our judgment, have to be rejected.

We do not understand that the doctrine enunciated in *Fosdick vs. Schall*, *supra*, was based merely or mainly upon the urgency of the need of the railway for the labor, supplies or equipment to which a preference is accorded. Nor do we apprehend that the mere fact that the supplies, labor or equipment furnished may have augmented the value of the bondholders' security, gives rise to a preference. In the light of *Fosdick vs. Schall*, *supra*, and the other cases in which the supreme court and other courts have followed the main case, our understanding of the doctrine is that, within narrow limits, a court of equity having in its custody a railroad which is being foreclosed by its mortgage creditors may make preferential payment of such claims, as debts due to operatives, limited amounts due to connecting roads for unpaid freight and ticket balances, limited amounts due for supplies needed from day to day or from month to month in the ordinary course of the railroad's operations. The controlling principle appears to be that a railroad having public duties to discharge must be kept a going concern while in the hands of the court, and that to that end debts due its employees and other current debts due for its ordinary operations, and which it is not usually practicable to pay for in cash, and which are, therefore, payable on short terms, should be paid as they would 855 have been paid if the court had not taken away from the corporation the control of the railroad. A cessation of the railroad's operations by failure to pay promptly the operatives or such other debts as railroads must necessarily incur from their ordinary current operations, must be prevented.

The payment of preferential debts included within the narrow limits indicated operates no impairment of the bondholders' rights, for it is made both in the interests of the property and of the public.

One purpose is to preserve the property in such condition that it may be sold as a growing concern, and thus may suffer no diminution of value while in the hands of the court. This is to the direct benefit of all creditors. The other purpose is to enable the railroad to continue the performance of its public duties. Of this the creditors will not be heard to complain, because they are charged with knowledge of the public obligations of their debtor.

In *Finance Co. vs. Charleston C. & C. R. Co.*, 62 F. R., 205, the circuit court of appeals for the fourth circuit, through Mr. Chief Justice Fuller, after stating certain debts which may be paid by preference, says: "Of course, the discretion to enter such orders should be exercised with great care." The Chief Justice then refers to the case of *Thomas vs. Western Car Co.*, 149 U. S., 95, as indicating the narrow limits within which a court of equity should confine itself in making preferential payments over railroad mortgagees.

In *Thomas vs. Western Car Co.*, just cited, the Supreme Court quoted approvingly from *Kneeland vs. American Loan Co.*, 136 U. S., 88, where it was said:

"The appointment of a receiver vests in the court no absolute control over the property, and no general authority to displace vested contract liens. Because in a few specified and limited cases, this court has declared that unsecured claims were entitled to priority over mortgage debts, an idea seems to have obtained that a court appointing a receiver acquires power to give such preference to any general and unsecured claims. It has been assumed that a court appointing a receiver could rightfully burden the mortgaged property for the payment of any unsecured indebtedness. Indeed, we are advised that some courts have made the appointment of a receiver conditional upon the payment of all unsecured
856 indebtedness, in preference to the mortgage liens sought to be enforced. Can anything be conceived which more thoroughly destroys the sacredness of contract obligations? One holding a mortgage debt upon a railroad has the same right to demand and expect of the court respect for his vested and contracted priority as a holder of a mortgage on a farm or lot. So, when a court appoints a receiver of railroad property, it has no right to make that receivership conditional on the payment of other than those few unsecured claims which, by the rulings of this court, have been declared to have an equitable priority. No one is bound to sell to a railroad company or to work for it, and whoever has dealings with a company when property is mortgaged, must be assumed to have dealt with it on the faith of its personal responsibility, and not in expectation of subsequently displacing the priority of the mortgage liens. It is the exception, and not the rule, that such priority of liens can be displaced."

In *Thomas vs. Western Car Co.*, *supra*, the Supreme Court proceeded to say:

"The case of a corporation for the manufacture and sale of cars dealing with a railroad company whose road is subject to a mortgage securing outside bonds, is very different from that of a workman and employees, or of those who furnish, from day to day, sup-

plies necessary for the maintenance of the railroad. Such a company must be regarded as contracting upon the responsibility of the railroad company, and not in reliance upon the interposition of a court of equity."

In *Kneeland vs. American Loan Co.*, *supra*, it is said

"It is the exception, and not the rule, that such priority of liens can be displaced. We emphasize this fact of the sacredness of contract liens, for the reason that there seems to be growing an idea that the chancellor, in the exercise of his equitable powers, has unlimited discretion in this matter of the displacement of vested liens."

In *Bound vs. S. C. R'y Co.*, 58 F. R., 473, the circuit court of appeals for the fourth circuit, Mr. Chief Justice Fuller sitting as a member of the court, in a case almost identical with the present case, said:

"The Supreme Court has recently in *Thomas vs. Car Co.*, 149 U. S., 95, indicated the narrow limits to which an equity
857 court should confine itself in allowing any unsecured claim to displace vested contract liens. Wages due employees, current operating expenses, current balances of ticket and freight money arising from indispensable business relations and similar current debts accruing within 90 days, are recognized as among the limited class of claims which in its discretion the court may allow to have priority. In the case cited the Supreme Court held it error to allow a claim for the rental of cars necessary to operate the road for the six months prior to the receivership."

Bound vs. S. C. R'y Co., *supra*, has been cited by the circuit court of appeals for the fourth circuit, in *Finance Co. vs. Charleston, etc.*, Co., 62 F. R., 208; by Circuit Judge Simonton in *Central Trust Co. vs. Charlotte C. & A. R. Co.*, 65 F. R., 269, and by Circuit Judge Colt in *Wood vs. N. Y. & N. E. R. R.*, 70 F. R., 743.

It would subserve no useful purpose to cite more extensively from the numerous authorities which show the narrow and restricted limits within which, in cases such as the matter in hand, preferential payments can be made. No case has been cited nor has any come under our observation in which such a claim as that of the Lackawanna Co. has been on final adjudication allowed a preference.

The case of *Burnham vs. Bowen*, *supra*, relied on by the intervenor's counsel and claimed to be analogous in principle to the instant case, was based on a demand for coal used in running the locomotives, supplied to the railroad company a few months before the appointment of a receiver, and the claim was found by the Supreme Court to be "one of the current debts for operating expenses made in the ordinary course of continuing business." We discover no similarity of principle between that case and the case at bar. Coal is an article of constant and uninterrupted consumption on a railroad, and its purchase at short intervals, for the purpose of running the locomotives in quantities not exceeding the operating requirements of the road are clearly current expenses of the road. But it is difficult to see how the purchase of 20,000 tons of rails

made under the circumstances stated in the intervenor's own pleadings can be a current debt "for operating expenses made in
858 the ordinary course of continuing business." If the road was in the condition of dilapidation, which is inferable from the intervenor's averments, it might be sufficient to say, in denying the demand that the rails were supplied, not as a matter arising in the ordinary course of a railroad's operations, but for the virtual reconstruction of the road. No authorities need be cited to establish the proposition that works of reconstruction are not entitled to preferential payment.

That the necessity for the supplies does not entitle to preferential payment unless the supplies are for the current expenses in the ordinary course of operation, is forcibly shown by the case of Morgan's L. & T. R'y Co. *vs.* Texas Central R'y Co., 137 U. S., 171, in which it was substantially held that the mere fact that money was loaned to a railroad company to pay the interest on its first-mortgage bonds, does not entitle the lender to preference, and that although advances of money may have enabled a railway company to maintain itself, that fact alone does not entitle the lender to priority. The contention that the intervenor is entitled to preference, because the rails supplied to it must have enhanced the value of the bondholders' security, is clearly untenable. In *Railway Co. vs. Cowdry*, 11 Wall., 482, Mr. Justice Bradley, as the organ of the court, said :

"As to the point of giving priority to the last creditor for aiding to conserve the thing, all that is necessary to say is, that the rule referred to has never been introduced into our laws except in maritime cases which stand on a particular reason." Also see *Thompson vs. White Water Valley R. R.*, 132 U. S. 68; *Jones on Corporate Bonds and Mortgages*, sec. 584; *Fogg vs. Blair*, 133 U. S., 534; *Toledo R. R. Co. vs. Hamilton*, 134 U. S., 296.

The unusually large purchase of rails, the time within which they were to be delivered, the condition of the road, the contracts providing for notes at six months renewable for a like term at the maker's option, the hypothecation of securities for the payment of the claim, the knowledge which the intervenor had of the mortgage, the fact that the contracts contained no promise to pay out of any particular fund, the time which elapsed between the date of the contracts and the appointment of a receiver in cause No. 185—are circumstances which, taken together, cannot fail to convince
859 us that the intervenor relied upon the general credit of the railway company.

We see no error in the action of the circuit court in dismissing the petition of intervenor and the decree appealed from is, therefore, affirmed.

I, J. M. McKee, clerk of the United States circuit court of appeals, for the fifth circuit, do hereby certify that page 1, pages 8 to 78, inclusive, pages 565 and 566, pages 572, 573, 574 and 575, pages 587 to 610, inclusive, pages 616 to 687, inclusive, page 825, and pages 840 to 859, inclusive, of the foregoing transcript, contain a true, full,

and perfect transcript of the record of cause No. 503, wherein The Lackawanna Iron & Coal Company *et al.* were appellants and The Farmers' Loan & Trust Company were appellees, as fully and completely as the same now remains on file and of record in my office.

In testimony whereof, I hereunto subscribe my name and affix the seal of said United States circuit court of appeals, for the fifth circuit, at the city of New Orleans, this 16th day of June, A. D. 1897.

[Seal United States Circuit Court of Appeals, Fifth Circuit.]

J. M. McKEE,

*Clerk of the United States Circuit Court of Appeals
for the Fifth Circuit.*

860 Circuit Court of Appeals, Fifth Circuit.

LACKAWANNA IRON & COAL CO. ET AL., Appellants, }
vs. } No. 503.
FARMERS' LOAN & TRUST CO. ET AL., Appellees. }

A writ of certiorari having been granted The Lackawanna Iron & Coal Company and The Pacific Improvement Company, appellants in the above cause, commanding that the record and proceedings therein be sent to said Supreme Court without delay, and it appearing that said appellants filed a true and correct copy of the record and proceedings had in said cause in this court and in the circuit court as part of and with the application for certiorari, and which copy is now on file in said Supreme Court—

It is therefore agreed that the said certified copy of the record and proceedings on file in the Supreme Court may be taken as a return to the writ of certiorari, and that this agreement be filed in the circuit court of appeals, so that the clerk may send up a copy thereof with his return to said writ and may in and be his said return make said certified copy of said record now on file in the Supreme Court a part of his said return.

[Seal United States Circuit Court of Appeals, Fifth Circuit.]

E. B. KRUTTSCHNITT,

Solicitor for Appellants and Applicant for Writ of Certiorari.

L. W. CAMPBELL,

Solicitor for Appellees Moran Bros. & McHarg.

M. F. MOTT,

Solicitor Farmers' Loan & Trust Co.

861 [Endorsed:] No. 503. Circuit court of appeals, fifth circuit. Lackawanna Iron & Coal Co. *et als.*, appellants, vs. Farmers' Loan & Trust Co. *et als.*, appellees. Stipulation as to return to certiorari.

862 United States Circuit Court of Appeals, Fifth Circuit.

I, J. M. McKee, clerk of the United States circuit court of appeals for the fifth circuit, do hereby certify that the foregoing page con-

tains a true copy of the stipulation as to return to certiorari in case of Lackawanna Iron & Coal Company *et als.*, appellants, *vs.* Farmers' Loan & Trust Company *et als.*, appellees, No. 503, as the same remains upon the files and records of said United States circuit court of appeals.

Seal United States Circuit
Court of Appeals, Fifth
Circuit.

In testimony whereof I hereunto subscribe my name and affix the seal of said United States circuit court of appeals, at the city of New Orleans, this 17th day of March, A. D. 1898.

J. M. McKEE,

*Clerk of the United States Circuit Court of
Appeals for the Fifth Circuit.*

863 UNITED STATES OF AMERICA, *ss.* :

The President of the United States of America to the honorable the judges of the United States circuit court of appeals for the fifth circuit, Greeting:

[Seal of the Supreme Court of the United States.]

Being informed that there is now pending before you a suit in which The Lackawanna Iron & Coal Company *et al.* are appellants and The Farmers' Loan & Trust Company *et al.* are appellees, which suit was removed into the said circuit court of appeals by virtue of an appeal from the circuit court of the United States for the eastern district of Texas, and we being willing for certain reasons that the said cause and the record and proceedings therein should be certified by the said circuit court of appeals and removed into

864 the Supreme Court of the United States, do hereby command you that you send without delay to the said Supreme Court, as aforesaid, the record and proceedings in said cause, so that the said Supreme Court may act thereon as of right and according to law ought to be done.

Witness the Honorable Melville W. Fuller, Chief Justice of the United States, the 26th day of October, in the year of our Lord one thousand eight hundred and ninety-seven.

JAMES H. McKENNEY,

Clerk of the Supreme Court of the United States.

865 [Endorsed:] Case No. 16,664. Supreme Court of the United States. No. 162, October term, 1898. The Lackawanna Iron & Coal Co. *et al. vs.* The Farmers' Loan & Trust Co. *et al.* Writ of certiorari and return. Office Supreme Court U. S. Filed Mar. 19, 1898. James H. McKenney, clerk.

The within writ received this March 17, 1898. In accordance with the agreement of counsel in the cause named in the within writ filed in the office of the clerk of the United States circuit court of appeals for the fifth circuit, a certified copy of which is hereto attached and made a part of this return, this writ is now returned

to the Supreme Court of the United States, and I, J. M. McKee, clerk of said United States circuit court of appeals, do hereby certify that the transcript of record in the within-named cause now on file in the Supreme Court of the United States is a true, full, and perfect transcript of the record, as fully and completely as the same now remains of record and on file in my office.

Seal United States Circuit
Court of Appeals, Fifth
Circuit.

In testimony whereof I hereunto subscribe my name and affix the seal of said United States circuit court of appeals, at the city of New Orleans, this 17th day of March, A. D. 1898.

J. M. McKEE,
*Clerk of the United States Circuit Court of
Appeals for the Fifth Circuit.*

Endorsed on cover: Case No. 16,664. U. S. circuit court of appeals, 5th circuit. Term No., 162. The Lackawanna Iron and Coal Company *et al.*, petitioners, *vs.* The Farmers' Loan & Trust Company *et al.* Petition for writ of certiorari and exhibit thereto. Filed September 4, 1897.

1897
U. S. COURT, U. S.
FILED
SEP 4 1897
JAMES H. MCKENNEY,
CLERK.

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1897.

No. ~~451~~ ~~452~~ 22

THE LACKAWANNA IRON AND COAL COM-
PANY Et AL., PETITIONERS,

versus

THE FARMERS' LOAN AND TRUST COM-
PANY Et AL., RESPONDENTS.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES
CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT.

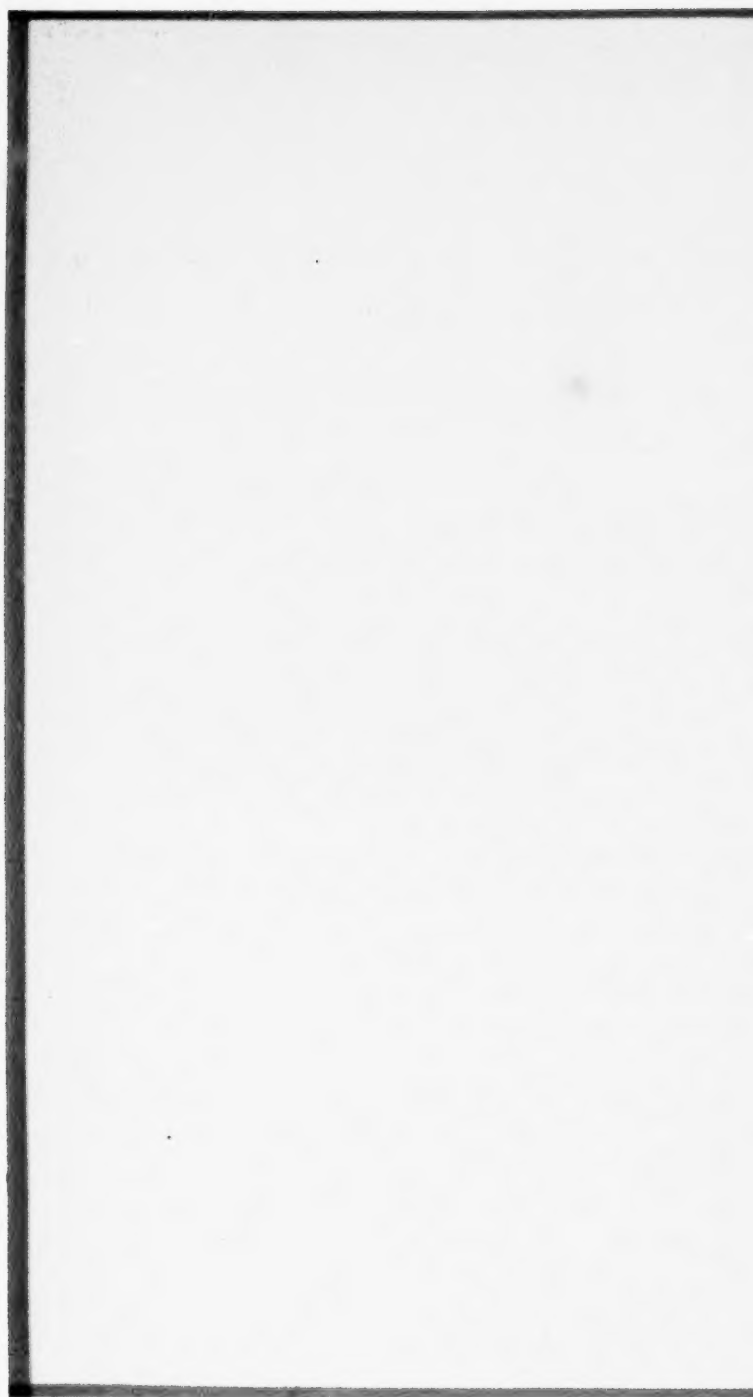
E. B. KRUTTSCHNITT,

E. H. FARRAR,

B. F. JONAS,

H. T. GURLEY,

J. W. Ashley
*Solicitors and of Counsel for Lackawanna Iron and
Coal Company, and for Pacific Improve-
ment Company.*



SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1897.

No.

THE LACKAWANNA IRON AND COAL COM-
PANY ET AL., PETITIONERS,

versus

THE FARMERS' LOAN AND TRUST COM-
PANY ET AL., RESPONDENTS.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES
CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT.

*To the Honorable the Justices of the Supreme Court of the
United States of America:*

The petition of the Lackawanna Iron and Coal Company, a corporation organized under the laws of the State of Pennsylvania, and a citizen of said State, and of the Pacific Improvement Company, a corporation organized under the laws of the State of California, and a citizen of said State, respectfully represent to your Honors, as follows :

I.

That on the 26th day of April, 1883, the said Lackawanna Company entered into a contract, in writing, with the Houston and Texas Central Railway Company, a cor-

poration organized under the laws of the State of Texas, and having its principal place of business at Houston, in said State, pursuant to which contract it delivered to said Railway Company five thousand and nine (5009) tons of 56-pound steel rails during the months of June, August and September, 1883, at the price of \$39.50 per ton. Pursuant to the terms of the contract, notes were issued in payment of these rails, aggregating in amount, with interest to their maturities, \$201,346.64; but which notes were from time to time renewed until they were reduced to eight in number, maturing at dates between January 20th, 1885, and April 24th, 1885, and aggregating in amount \$118,000. (Master's Report, R. pp. 651-2).

II.

Under another contract entered into between the Lackawanna Company and the said Railway Company on the 30th day of October, 1883, the Lackawanna Company delivered to said Company 8552 tons of 54 lb. steel rails during the months of February, March, April and May, 1884, the purchase price of which rails, evidenced by promissory notes maturing at different dates during the months of February, March, April and May, 1895, amounted to \$327,175.50. (Master's findings, R. pp. 653-4).

III.

Of the rails furnished under the first of said contracts, and under a contract prior in date to said first contract, a portion was laid upon the tracks of the railway of the Waco and Northwestern Division of said Houston and Texas Central Railway Company. Said portion was suffi-

cient to lay 6.2 miles of said railway of said division, and was laid upon the same; and although it is impossible to show exactly what proportion of said rails were furnished under each of said two contracts, it is fair and equitable to prorate said rails between said two contracts, for the reason that the quantity of rails furnished under the said prior contract and under said contract of April 26th, 1883, was about equal, and that said Waco and Northwestern Division was run as a part of the general railway system of the Houston and Texas Central Railway Company, so that it is, in many matters, including the one now under consideration, impossible to separate its accounts from those of the rest of the system. The original contract price of the 5009 tons of rails furnished under said contract of April, 1883, was \$197,855.50, which was reduced by payments to \$118,000, as aforesaid; the said rails weighed 56 pounds to the yard, so that the rails laid on 3.1 miles of road amounted to 272.8 tons, which, at the contract price of \$39.50 per ton, were worth \$10,775.60. (Master's Report, R. p. 655).

The *pro rata* of the payments made under said contract of April 26, which would be imputable to said amount of \$10,775.60, is \$4449.09, and reduces the said amount to \$6426.51, which is the balance due upon the contract price and value of the rails furnished by the Lackawanna Company under the said contract of April 26, and laid upon the railways of the Waco and Northwestern Division of the Houston and Texas Central Railway Company.

IV.

Of the rails furnished under the second of said contracts,

viz: the one of October 30, 1883, an amount sufficient to lay 30.8 miles was used upon the railways of the Waco and Northwestern Division of the Houston and Texas Central Railway. The contract price of the rails was \$36.60 per ton; 84.86 tons of 54-pound rails are needed to lay one mile of track, so that the value of the rails delivered under said last-named contract, and laid on said Division, was, at the contract price, ~~\$90,200.64~~. (Master's Report, R. pp. 655, 656).
 95,660.98

V.

At the time when the Lackawanna Company made the contracts and furnished the rails aforesaid, the condition of the track of the defendant Company was such that the demand for new rails upon the most worn portion of the same was practically imperative. The road north, from Houston, for 90 miles, was completed between 1857 and 1861, and thence northward to Denison between 1867 and 1872. The Waco and Northwestern Division was completed about 1875. The condition of the road was bad. There was continual breakage of rails and wreckage of trains; the track was unsafe, and was generally so regarded not only by railroad men, but by the traveling public; the damage to merchandise, rolling stock, etc., was continuous, and new rails were absolutely essential for the preservation of human life, the loss of which was liable to occur at any moment. Both buyer and seller expected the rails to be paid for from the current earnings of the railway. The sale was made without any stipulation for security to be given by the said Railway Company, or for payment out of any particular fund, or in any particular

way. (See Master's Report, Rec. pp. 656-7, differing slightly but not substantially from this statement).

The rails supplied under these contracts were laid in the tracks of the said Railway Company as above stated. (See Master's Report, Rec. *locis citatis*).

VI.

About nine months after the last of these rails were delivered, a Bill of Complaint was filed in the United States Circuit Court for the Eastern District of Texas by the Southern Development Company, praying, among other things, for the appointment of Receivers to all the railways of the Houston and Texas Central Railway Company (Master's Report, R. pp. 653 and 658), including the railways of said Waco and Northwestern Division.

Upon this bill, Benjamin G. Clarke and Charles Dillingham were appointed Receivers on the 21st day of February, 1885. This bill was filed by the Southern Development Company, seeking a marshaling of the assets of the said Railway Corporation, and a declaration that the claim of said Company was secured by a lien upon the net earnings of the Railway Company, and upon all of its property, superior in rank to the mortgage bonds. It was filed by the Southern Development Company in its own behalf, and in behalf of all other persons similarly situated, who might intervene to protect their own interests. The Lackawanna Company did intervene, praying substantially for the same relief as is prayed for by its intervention in Cause No. 227 of the docket of the United States Circuit Court for the Eastern District of Texas, hereinafter more fully referred to. (Master's Report, Rec. pp. 659-668).

The Bill of Complaint of the Southern Development Company was, on the 27th day of May, 1886, dismissed upon demurrer, without prejudice to the rights of complainants to assert their claims, if any they had, in such manner as they might be advised; but prior to the dismissal of said bill, Nelson S. Easton, James Rintoul and Charles Dillingham were appointed Receivers of the properties of the said Railway Company, including the said Waco and Northwestern Division, under three bills filed by various mortgage creditors, and which bills are generally known as Bills Nos. 198, 199 and 201 of the Chancery Docket of the Circuit Court of the United States, for the Eastern District of Texas. (Master's Report, R. p. 662).

VII.

Clarke and Dillingham, Receivers, turned over all the property in their possession to Easton, Rintoul and Dillingham, as Receivers, on the 10th of July, 1886, and these Receivers remained in possession of the property until December 7th, 1888, or thereabouts, when Easton and Rintoul were relieved from further duty, and Dillingham continued as sole Receiver. (Master's Report, R. p. 663).

The mortgages declared upon in the Causes Nos. 198, 199 and 201 were foreclosed by final decree entered in Consolidated Cause No. 198, under which number the three causes, together with others, had been consolidated, and under this decree all the property of the Railway Company was sold on the 8th of September, 1888, including the property of the Waco and Northwestern Division of the Houston and Texas Central Railway, which property, however, was sold subject to the mortgage forming the subject

matter of the bill of foreclosure of the Farmers' Loan and Trust Company, filed under the No. 227 of the docket of the United States Circuit Court for the Eastern District of Texas, which will be hereinafter more fully referred to, and subject, also, to the right which the Court reserved by its decree to charge upon the property, or any part thereof, the payment of any amount that might be found to be due and payable by reason of intervening petitions theretofore filed in said cause, and to be entitled to priority over the mortgage debts referred to in the decree. (Master's Report, R. p. 663).

The Lackawanna Company had, long prior to said decree, filed its petition of intervention in said Cause No. 198, praying substantially for the same relief as it had prayed for in its petition in Cause No. 185, and praying substantially for the same relief as it prays for in its petition of intervention in said Cause No. 227. (Master's Report, R. pp. 616 *et seq.*)

VIII.

Subsequently to the decree in said Cause No. 198 and to the sale made thereunder, the Lackawanna Company, on the 20th day of April, 1889, filed its petition in said Cause No. 198, asking that the Receivership therein should continue and remain over the property then in the possession of the Court, being the property now in the hands of the Receiver in said Cause No. 227, until the claims and demands of the Lackawanna Company should have been finally decreed upon, and if decreed in its favor, should have been finally paid and settled; and, further, praying the Court to render a preliminary order staying the order

which had theretofore been rendered, directing the delivery of the property to one George E. Downs, who had become the purchaser thereof, and directing the Receivers not to deliver the property to any purchaser until after the final hearing of the matter of said petition. (Master's Report, R. p. 675).

On this petition an order was rendered directing Downs and the Farmers' Loan and Trust Company to show cause why the relief prayed for should not be granted; and further directing the Receiver to retain possession of the property until the further order of the Court; and further ordering that the Receivership which had theretofore been ordered in Cause No. 227 should be concurrent with the original Receivership ordered in Cause No. 198, and that the Receiver should keep separate accounts of the earnings and expenses of the Waco and Northwestern Division of the Houston and Texas Central Railway Company. (Master's Report, R. p. 675).

It will thus be seen that ever since the Lackawanna Company filed its intervention in Cause No. 185, on the 12th day of September, 1885, the Lackawanna Company has at all times had an intervention pending in the matter of the Receivership of the Waco and Northwestern Division of the Houston and Texas Central Railway Company in every phase which that litigation has assumed. It will be seen that the Receivership ordered in Cause No. 198 has been continued concurrently with the Receivership in Cause No. 227, down to the present day. Thus, any intimation of laches, or of sleeping upon rights, is conclusively disproved, in so far as the conduct of the Lackawanna Company, itself, is concerned.

IX.

That the Southern Development Company filed its said Bill in suit No. 185 of the docket of the United States Circuit Court for the Eastern District of Texas on the 16th day of February, 1885. It filed an Amended and Supplemental Bill on the 18th day of April, 1885, after the appointment of Receivers. Prior to the filing of this Amended Bill, on March 31, 1885, the Farmers' Loan and Trust Company filed its petition in said Cause No. 185, praying to be made a party thereto, averring among other things that it was trustee under several different mortgages executed by the defendant Railway Company, and naming among others the mortgages subsequently sued upon in Cause No. 227. The prayer of the petition was granted on April 6, 1885; the Farmers' Loan and Trust Company was allowed to become a defendant in said suit No. 185, with a proviso that it might demur, plead or answer on or before the Rule Day in June, 1885. On June 15, 1885, pursuant to this leave, the Farmers' Loan and Trust Company answered both the Original and Supplemental Bill of the Complainant; the averments of said answer are all defensive, and this answer, with the petition praying to be made a party defendant, are the only pleadings and appearance made by the Farmers' Loan and Trust Company in Cause No. 185, and it does not appear from said answer that the Farmers' Loan and Trust Company, as trustee for any of the mortgages mentioned in said answer, either demanded of the Court that the Receiver should hold the property for said trustee, or in any other manner demanded affirmative relief under any of the mortgages under which it was a trustee. (Master's Re-

port, R. pp. 671-2). Its appearance in said Cause No. 185 was simply that of a defendant in opposition to the rights asserted in the original and supplemental bill of complaint.

X.

The bill in Cause No. 195 was, as aforesaid, dismissed upon demurrers, which demurrers were filed on October 5th, 1885, by Easton and Rintoul, Trustees, under various mortgages. This dismissal occurred May 27th, 1886 (R. p. 672); but on May 26th, 1886, prior to the entry of the order of dismissal, on motion of the defendant, the Houston and Texas Central Railway Company, an order was rendered in six causes, numbered respectively 183, 184, 188, 198, 199 and 201. This order was rendered upon consent of all parties in open Court. It first provided that no further proceedings should be had in Causes Nos. 183, 184 and 188, without notice to the Railway Company. It further provided that Causes Nos. 198, 199 and 201 should be consolidated under the No. 198, and under the name and style of Nelson S. Easton and James Rintoul, Trustees, and the Farmers' Loan and Trust Company, Trustee, against the Houston and Texas Central Railway Company, and Benjamin A. Shepard, Trustee, Consolidated Cause; that in said cause Easton and Rintoul should stand as complainants, as trustees under the mortgages or deeds of trust made by the defendant Railway Company, and bearing dates respectively July 1st, 1886, and December 21st, 1870; that the Farmers' Loan and Trust Company, expressly assenting thereto, should stand as complainant under the mortgages or deeds of trust made by the defendant Railway Company, bearing dates respectively June

16th, 1873, October 1st, 1875, and April 1st, 1881, and that Benjamin A. Shepard should stand as defendant, as trustee under the mortgage or deed of trust made by the defendant Railway Company, bearing date May 7th, 1877; that the bills filed in said Causes Nos. 198, 199 and 201, should stand as bills in the Consolidated Cause, and might be amended by either complainant, as they might be advised, by the August Rule Day, and that any party might file an answer to such original or amended bills as he might be advised within thirty days after said August Rule Day. No other action was taken in Causes Nos. 183, 184 and 188, after the order above mentioned, and it is unnecessary to further allude to them. Consolidated Cause No. 198 proceeded to final decree, and the three mortgages declared on therein were in all things foreclosed. (Master's Report, R. p. 673).

The Farmers' Loan and Trust Company, in its capacity as Trustee, in the mortgage declared upon in Cause No. 227, expressly assented to stand as complainant in said Cause No. 198, but filed no Bill of Complaint therein, in its said capacity, and the Bill of Complaint in Cause No. 227 was not filed until long after final decree in Cause No. 198.

XI.

Prior to March, 1887, Easton and Rintoul filed a petition in Cause No. 198, seeking an order directing the Receivers, out of surplus earnings of the Railway Company in their hands, to pay the interest coupons due upon mortgages whereof they were trustees.

On March 21st, 1887, the Farmers' Loan and Trust Company filed an answer to the said petition of Rintoul

and Easton, wherein and whereby the Farmers' Loan and Trust Company, as Trustee, under the Waco and Northwestern First Mortgage, being the mortgage forming the subject matter of Bill No. 227, prayed the Court that any order which should be rendered in Cause No. 198, directing the payment by the Receivers out of the surplus of net earnings in their hands of any coupons falling due upon mortgages secured by any of the trust deeds by said Railway Company, might also order and provide for payment by the Receivers out of the surplus of net earnings in their hands of the two coupons due upon the Waco and Northwestern Division first mortgage, as well as upon the said other first mortgages. (Master's Report, R. p. 673).

The application of Easton and Rintoul, as also the application of the Farmers' Loan and Trust Company, for the payment of interest coupons, on the bonds secured by first mortgages or deeds of trust, described in the Bills of Complaint in said Consolidated Cause, came on to be heard on the 27th day of April, 1887, when an order was rendered by the United States Circuit Court for the Eastern District of Texas, that the coupons due January 1, 1885, and July 1, 1885, upon the first mortgage bonds of the Waco and Northwestern Division of the Houston and Texas Central Railway should be paid, as provided in the order, with interest. The two coupons were paid pursuant to this order. The order expressly declared that it was:

"Without prejudice to the rights of defendant or any intervenor in this cause, or any final decree to be rendered in the same, nothing herein being decided as to the merits of the claim of the defendants, or of intervenors, and this order not in any manner stopping or affecting the rights of any party or intervenors in this cause."

The Farmers' Loan and Trust Company, as Trustee upon this same first mortgage of the Waco and Northwestern Division, also filed petitions in the United States Circuit Court for the Eastern District of Texas, on the 6th day of November, 1888, and on the 20th day of November, 1888, for payment of the remaining coupon interest due upon the first mortgage of the Waco and Northwestern Division, upon which petitions no order was ever rendered. (Master's Report, Rec. p. 674).

XII.

By the final decree, rendered in Cause No. 198 on the 4th day of May, 1888, foreclosing the various mortgages sought to be foreclosed in said cause, the United States Circuit Court for the Eastern District of Texas expressly reserved the right to charge the property, under said decree ordered to be sold, with any amounts that it might decree in favor of any interventions then on file, and the intervention of the Lackawanna Company was on file at the time of said decree. (Master's Report, R. p. 674).

XIII.

The amount of the coupons and interest paid to holders of first mortgage bonds of the Waco and Northwestern Division, under the orders of Court above referred to, including the interest paid pursuant to said orders, amounted to \$91,371. (R. p. 680).

XIV.

During the years 1883 and 1884, while the rails were being furnished to the Houston and Texas Central Railway Company, that Company paid out \$2,386,400 in inter-

est upon its bonded indebtedness; which amount, less \$1,043,198.27, which was borrowed for interest purposes, in those years, was paid from income or current earnings. Out of this amount \$159,600 was paid as interest on the first mortgage bonds of the Waco and Northwestern Division, being the bonds forming the subject matter of the Bill of Complaint in Cause No. 227. (Master's Report, R. p. 676).

XV.

During the Receivership of Clarke and Dillingham, in Cause No. 185, they received from the operations of the railway of the defendant Company a total of . . \$4,902,218 45
 Their expenditures for operating expenses,
 taxes, etc., for the same period, amounted to . . 3,479,076 29

Leaving a net balance from the operations of the railways of the Houston and Texas Central Railway Company, from February 23, 1885, to July 10, 1886, in cash, of \$ 423,142 16

These figures are the result of a consolidation of the figures given at p. 666 of the Record in the Master's Report.

XVI.

The Receivers, in Suits Nos. 185 and 198, Clarke, Dillingham, Easton and Rintoul, during their administration, expended a sum total of \$1,538,116.38 outside of operating expenses, all of which, except the sum of \$23,274.20, clearly went into the pockets of the mortgage creditors, or was expended in betterments upon the properties mortgaged to them. In other words, a total of \$1,512,842.18 inured out of the revenues of the Receivership to the benefit of the mortgage creditors. (Master's Report, Rec. p. 667).

XVII.

The accounts of the Railway Company were not kept in such a manner as to distinguish between earnings and expenses on the Waco and Northwestern Division, and those derived from the other divisions of defendant Company's Railway. (Master's Report, Rec. p. 680).

XVIII.

The properties mortgaged to the Farmers' Loan and Trust Company, under the mortgages sought to be foreclosed in this cause, were the lines of the Houston and Texas Central Railway, from Bremond to Ross, commonly known as the Waco and Northwestern Division, extending a distance of fifty-eight miles, whilst all the roads of the Houston and Texas Central Railway Company, including the Waco and Northwestern Division, amount to a total mileage of 521 $\frac{3}{4}$ miles. (Bill of Complaint, R. p. 9). In other words, the Waco and Northwestern Division constitutes 11 13-100 per cent. of the whole system.

XIX.

The indebtedness due by the Houston and Texas Central Railway Company to the Lackawanna Company was liquidated by judgment of the District Court of Dallas County in suit instituted by the Lackawanna Company against the defendant Railway Company, at the sum of \$555,914.25, with interest at eight per cent. per annum from May 17th, 1889 (Master's Report, R. p. 676), and upon this judgment execution issued August 19th, 1889, which was returned by the Sheriff of Dallas County, not executed, there being no property found in Dallas County, subject to execution. (Master's Report, R. p. 670).

XX.

On the 6th day of April, 1889, the Farmers' Loan and Trust Company, as complainant, filed a Bill of Complaint against the Houston and Texas Central Railway Company and others, seeking the foreclosure of the first mortgage granted by the latter Company upon the division of its railways, known as the Waco and Northwestern Division. (Rec. pp. 8 *et seq.*) This suit is numbered 227 of the docket of the U. S. Circuit Court for the Eastern District of Texas.

XXI.

In this proceeding the Lackawanna Iron and Coal Company filed a petition of intervention, the object of which petition was to obtain the recognition of the indebtedness due to it by the Houston and Texas Central Railway Company, as aforesaid.

This petition (R. pp. 623 *et seq.*) asked that an account might be taken, under the direction of the Court, as to the dates and amounts of money paid by the defendant Railway Company to any of the mortgagees in the various trust deeds, described in the petition, showing particularly the issue of bonds upon which such interest was paid; and what proportion of the amounts so paid were paid out of current revenues of the Company, in the absence of earnings, and what amounts were so paid out of net earnings of the defendant Railway Company; and particularly so as to show what amounts and proportions were so paid out of the net earnings of those portions of the railway of the defendant Railway Company, described in the Bill of Complaint of the Farmers' Loan and Trust Company, herein-

above referred to; that an account might be taken showing the proportion of steel rails furnished by petitioner to the defendant Railway Company, used upon the railways described in the Bill of Complaint; and that the account to be taken should also show all receipts and expenditures made by the Receivers, in whose hands the property had been placed under proceedings which will be hereinafter at greater length detailed, and which account should be taken in such manner as to show the dates when the expenditures were made, and the character of the expenditures, and in such manner as to show whether the expenditures were made for operating and running expenses, or for extraordinary repairs, betterments and improvements of the property, and for the payment of fixed charges upon the same.

Said petition further prayed that for the amounts due on such accounting to petitioner and equitably chargeable upon the railways described in the Bill of Complaint in said cause, there might be a decree against the defendant Railway Company, and against all of the parties complainant and defendant, decreeing the sum so due to be liens upon the net earnings of the Railway Company, and especially upon those portions of said net earnings which have accrued or may accrue from the railways described in the Bill of Complaint, both those accrued prior to the Receivership in Cause No. 185, and those accrued and to accrue during the Receivership in Cause No. 198; and upon all of the property of the Railway Company, superior in rank to the claims of the trustee and of the holders of mortgage bonds and coupons issued under the deed of trust sought to be foreclosed by the Farmers' Loan and Trust Company; that the net earnings of the railway described in the Bill of

Complaint should be first devoted to the payment of the amounts so decreed, and, if they should prove insufficient to pay the amounts, then that the Court should decree the payment of said amounts out of any proceeds of sale of the property of the Railway Company to be made under final decree.

XXII.

To this petition an answer was filed by the Farmers' Loan and Trust Company, which covers ten pages of the Record (pp. 635 *et seq.*), which is substantially a denial of all equities of the Lackawanna Iron and Coal Company, and of the facts upon which the same are alleged to exist.

Moran Bros. and Henry K. McHarg, bondholders, subsequently intervened and pleaded that the petition of intervenors was barred by the Statute of Limitations, in addition to which they adopted the answer of the Farmers' Loan and Trust Company. (Rec. pp. 647-8).

XXIII.

The Pacific Improvement Company, as assignee of the Lackawanna Company, was, by order of Court, and upon its petition, made a co-petitioner with the Lackawanna Company. (R. p. 646).

XXIV.

The petitions, with the answers of the Farmers' Loan and Trust Company, and of Moran Bros. et als., intervening bondholders (R. pp. 635 and 647), was referred to William L. Prather as a special master "to take the accounts prayed for, and to investigate, find and report upon the facts as to the subject matter of said petition, and of the answers thereto."

XXV.

The facts of the case were found by the Master, as will be seen from his report, which will be found in the printed record of the United States Circuit Court of Appeals for the Fifth Circuit, of which copies are filed with and as part of this petition. The references hereinabove made to the record in support of the allegations of fact have been taken from said report, which gives the facts of the case in a succinct form, and which report was not excepted to by either party.

Upon the facts, as found by the Master, the intervention of the Lackawanna Iron and Coal Company came for trial before the Honorable the Circuit Court of the United States for the Eastern District of Texas, which Court dismissed said petition. (See Rec. p. 681).

XXVI.

The cause was taken by appeal to the Circuit Court of Appeals for the Fifth Circuit, which Court affirmed the decree of the lower court, as will be seen from a certified copy of said opinion. (R. pp. 844 *et seq.*)

Petitioners applied for a rehearing in said Court, which was refused. (R. p. 843). The propositions submitted to said Circuit Court of Appeals, under proper assignments of error, were the following, to-wit:

1.

That the claim of the Lackawanna Company is one of the character repeatedly recognized by the Supreme Court of the United States as a charge in equity on the continuing income of a railway company as well that which comes

into the hands of the Court after a receiver is appointed as that before, and that so far as this current expense creditor is concerned, the Court should use the income of the receivership in the way in which the Company would have been bound in equity and good conscience to use it, if no change in the possession had taken place ; and further, that if the income has been diverted from the payment of current income creditors to the payment of mortgage creditors, or to the improvement of the mortgaged property, the current income fund, to the extent to which it has been depleted, will be restored out of the proceeds of sale of the mortgaged property.

B.

That the Farmers' Loan and Trust Company and the beneficiaries under its trust never had a lien upon any of the earnings of the Waco and Northwestern Division of the Houston and Texas Central Railway Company, and they have no lien upon any such income now in the possession of the Circuit Court.

C.

If neither party has, nor at any time during the litigation under consideration had, a lien on the income of the railways mortgaged in this case, then the Court will proceed upon the principle that equality is equity, and will distribute the income ratably among all the creditors of the defendant Railway Company before the Court.

XXVII.

Said Honorable Circuit Court of Appeals, in its opinion,

held that the claim of petitioners is not one of the character recognized by this Honorable Court as a charge in equity on the continuing income of a railway company in manner and form, and to the extent set forth in the first of the foregoing propositions, and that the claim of petitioners was entitled to no priority under the doctrine laid down in the case of *Fosdick vs. Schall*, and a long line of decisions following, affirming, explaining and modifying said decision; and said Honorable Circuit Court of Appeals did not, by its opinion, pass upon either of the other points hereinabove set forth.

XXVIII.

The two important questions of law involved in said cause are:

(a) Whether or not a claim for rails furnished to a railway company, for the purpose of keeping it up as a going concern at a time when but for such furnishing its operations would practically cease, is a claim of the character which will, under the doctrine in *Fosdick vs. Schall*, be granted priority on the continuing income of a railway company as well that which comes into the hands of the Court after a receiver is appointed as that before, in the manner and form and to the extent set forth in the first of the said propositions; and whether this claim, if it existed, is lost by the acceptance of promissory notes and the giving of time to the embarrassed company.

(b) Whether or not a mortgagee has any lien upon the revenues of the mortgaged property accruing prior to the filing of a foreclosure bill, and during a receivership pro-

voked by others, and in proceedings wherein such mortgagee is a defendant only and not a complainant.

That the Honorable the Circuit Court of Appeals did not discuss this second question in its opinion, but by affirming the decree of the lower court necessarily affirmed the existence of such a lien.

XXIX.

Now, your petitioners aver that they are advised by counsel that this Honorable Court has never yet in any case directly passed upon the questions constituting the distinguishing features of this case and controlling its correct decision; that your petitioners are further advised that the scope and extent of the doctrine announced in the case of *Fosdick vs. Schall* will, within a very few weeks after the opening of the October Term of this Honorable Court, in 1897, undoubtedly become the subject matter of an adjudication by this Honorable Court in a cause wherein it has heretofore issued a writ of *certiorari* to the Honorable the Circuit Court of Appeals for the Fifth Circuit, said cause being the cause entitled *Rowena M. Clark et al. vs. The Central Railroad and Banking Company, of Georgia, et al.*, No. 100 of the Docket of this Honorable Court, for the October Term, 1897.

Your petitioners are further advised that the Honorable the Circuit Court of Appeals for the Fourth Circuit has, in the cause entitled *Southern Railway Company vs. Carnegie Steel Company, Limited*, reported in the *76th Federal Reporter*, 492, decided a cause in accord with the contentions of petitioners, and in diametrical opposition to the decision of the

Honorable the Circuit Court of Appeals for the Fifth Circuit, upon the claim of your petitioners.

That said cause, so decided by said Circuit Court of Appeals for the Fourth Circuit, is, as to nearly every crucial fact, an exact duplicate of the cause now presented to your Honors in this petition, and is its exact duplicate in law. Both causes involved two successive receiverships, to-wit: First, a receivership instituted, not at the suit of a mortgagee, but at the instance of other creditors, to protect the property from disruption and hold it together; and thereafter a supervening receivership, provoked by bondholders, and to which the first receivership was made to account. Both causes involved a claim for steel rails, involved a consideration of the effect to be given to the fact that promissory notes were given in evidence of a credit extended for said rails; involved renewals of the notes so given, and involved the alleged laches of the petitioners.

That your Honors have heretofore issued a writ of *certiorari* to the said Honorable the Circuit Court of Appeals for the Fourth Circuit, in the matter of the *Southern Railway Company vs. The Carnegie Steel Company, Limited*, which cause is now pending upon the Docket of this Honorable Court and is numbered 278 upon the Docket for the October Term, 1897.

Petitioners aver that the questions involved in this cause are of very great importance, and of a degree of general importance which should, your petitioners respectfully submit, obtain from your Honors a review of the said decision of the said Circuit Court of Appeals for the Fifth Circuit by, and on *certiorari*. That such hearing on

certiorari of this cause is essential, in order to maintain a uniformity of jurisprudence between different Circuit Courts of Appeal—the decisions of said Circuit Court of Appeals for the Fourth Circuit and said Circuit Court of Appeals for the Fifth Circuit being, as aforesaid, in diametrical opposition to each other.

Petitioners further aver that this application is prosecuted with due and with all possible diligence; that the decision of the said Honorable the Circuit Court of Appeals for the Fifth Circuit, of which your petitioners seek to obtain a review by *certiorari*, was rendered by said Court on the 25th day of February, 1897. That an application for a rehearing in said cause was, within the delay fixed by the rules of the said Honorable Circuit Court of Appeals, filed by petitioners on the 16th day of March, 1897. (Rec. pp. 841 *et seq.*) That the said application received the consideration of the said Circuit Court of Appeals, and was not denied until the 10th day of June, 1897, as will appear from the record herein. (Rec. p. 843).

That the act of said Circuit Court of Appeals for the Fifth Circuit, in holding said cause under consideration, although an act performed in the proper and orderly performance of the judicial duties of said Circuit Court of Appeals, produced the result that the decree of the said Honorable the Circuit Court of Appeals, although rendered several weeks prior to the adjournment of this Honorable Court in May, 1897, did not become final until after the said adjournment of this Honorable Court; that petitioner had therefore not exhausted its remedies in the lower court until subsequently to the adjournment of this Court in May, 1897, and that this petition is filed during the sum-

mer vacation of 1897, in order that it may be presented to your Honors at the opening of the October Term, 1897.

That owing to the inability of petitioners to present this application to your Honors immediately after the refusal of said rehearing, by reason of the fact that this Honorable Court was in vacation as aforesaid, the mandate of said Honorable Circuit Court of Appeals for the Fifth Circuit has issued to the Circuit Court of the United States for the Eastern District of Texas, and that petitioners desire that said mandate be recalled, as hereinafter prayed for.

Petitioners file herewith a copy of the opinion of the Court of Appeals (Rec. pp. 844 *et seq.*), copies of the record and of the briefs filed by them in said Court, and also a brief in support of this petition.

Wherefore, petitioners pray that a writ of *certiorari* may issue to the said Honorable the Circuit Court of Appeals for the Fifth Circuit to bring up, for review before your Honors, the judgment and decree of said Court, in the cause entitled *Lackawanna Iron and Coal Company et al., Appellants, vs. Farmers' Loan and Trust Company et al., Appellees*, No. 593 of the Docket of said Honorable Court; and that your Honors will issue an order directing said Honorable Circuit Court of Appeals to recall its mandate, and to hold the same subject to the orders and decrees of this Honorable Court, and until your Honors can hear and pass upon said writ of *certiorari*; and your petitioners pray, that on the hearing of said writ of *certiorari*, so to be issued, your Honors do quash and reverse the decree of said Circuit Court of Appeals for the Fifth Circuit, and do render a decree that petitioners be paid out of the funds in the

custody of the Court the two sums of sixty-two hundred and forty-six 51-100 dollars (\$6246.51), and ~~ninety-nine thousand three hundred 64-100 dollars (\$99,300.64)~~ ^{ninety-nine thousand 98-100 dollars (\$99,500.98)}, with interest at six per cent. per annum upon both of said amounts, from May 1st, 1885, until paid; or, if this Honorable Court should conclude that neither the Lackawanna Iron and Coal Company, nor the Farmers' Loan and Trust Company, as Trustee, has established any lien in the premises, then that this cause be remanded to the said Honorable the Circuit Court of Appeals, with instructions to remand the cause to the Circuit Court, and with instructions to the latter Court to distribute the income in the hands of said Circuit Court, after payment of all costs and expenses, *pro rata* between the different creditors of the Houston and Texas Central Railway Company before the Court; and petitioners pray for all such further and general relief in the premises as the case may require, and as in their petition of intervention prayed for, and as to your Honors may seem meet and just.

Respectfully submitted,

E. B. KRUTTSCHNITT,

E. H. FARRAR,

B. F. JONAS,

H. T. GURLEY, *H. T. Gurley*

Solicitors and of Counsel for Lackawanna Iron and Coal Company, and for Pacific Improvement Company.

STATE OF NEW YORK,)
 County of New York,)
 City of New York. }

Personally came and appeared before me, the under-
 signed authority *Edwin J. Hatfield* who, being

duly sworn, deposes and says, that he is the *President*
 of the Lackawanna Iron and Coal Company, one of the
 petitioners in the above petition, and that all the facts,
 matters and things therein set forth are true to the best of
 his knowledge, information and belief. *E. J. Hatfield*

Sworn to and subscribed before me

this *2d* day of *Sept* 1897.

(Seal) *Edwin F. Conroy,*

Notary Public, N. Y. Co.

STATE OF NEW YORK,)
 County of New York,)
 City of New York. }

Personally came and appeared before me, the under-
 signed authority *Thos. H. Hubbard* who, being

duly sworn, deposes and says, that he is the *Atty. Genl.*
 of the Pacific Improvement Company, one of the petitioners
 in the above petition, and that all the facts, matters and
 things therein set forth are true to the best of his knowledge,
 information and belief. *Thos. H. Hubbard*

Sworn to and subscribed before me

this *3d* day of *Sept* 1897.

(Seal) *William Shellaben.*

Notary Public, N. Y. Co.

454. 1892. 22.

FILED
OCT. 17 1897

JES. H. McKERN

of Kruttschnitt, Farrar,
Ashton for Petitioners.

Filed Oct. 11, 1897.

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1897.

No. . . 451

THE LACKAWANNA IRON AND COAL COMPANY
Et AL.

versus

THE FARMERS' LOAN AND TRUST COMPANY
Et AL.

BRIEF IN SUPPORT OF APPLICATION FOR A WRIT OF CERTI-
ORARI TO THE UNITED STATES CIRCUIT COURT OF
APPEALS FOR THE FIFTH CIRCUIT.

E. B. KRUTTSCHNITT,
E. H. FARRAR,
B. F. JONAS,
H. T. GURLEY,

Solicitors and of Counsel for Lackawanna Iron and
Coal Co. and for Pacific Improvement Co.

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1897.

No.

THE LACKAWANNA IRON AND COAL COMPANY
ET AL.

versus

THE FARMERS' LOAN AND TRUST COMPANY
ET AL.

BRIEF IN SUPPORT OF APPLICATION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT.

We have in a brief, written for the Circuit Court of Appeals, presented a statement of the facts, and of the law of this case, and we have filed the requisite number of copies of this brief with the petition for a writ of *certiorari*. This brief is submitted to your Honors in support of the application for a writ of *certiorari*.

We have, however, thought it well to also present a shorter and more condensed statement of the vital facts of the case with as little detail as possible, said statement to be followed up by a short statement of the propositions of law upon which we rely to obtain the writ.

Before we even state the case, we would say to your Honors that, although the transcript in this cause consists

of 833 printed pages, the whole of the case of the Lackawanna Iron and Coal Company will be found between pages 616 and 687, and that it will be unnecessary for your Honors to trouble yourselves with any other portions of the Record outside of the pages named, except possibly with the Bill of Complaint, and Mortgage or Deed of Trust thereto annexed. (Rec. pp. 8 *et seq.*)

STATEMENT OF CASE.

The Lackawanna Iron and Coal Company is, and has been, since the year 1883, a creditor of the Houston and Texas Central Railway Company, for steel rails furnished to said Company, under contracts, and in order to enable said Company to replace the old iron, with which its tracks were laid, and at a time when the rails were so absolutely necessary, that it was doubtful whether the Company could have maintained its existence as a common carrier without them. Prior to the improvement and repair of the line of road with said rails, accidents to life and limb, and damage to property, were so great, owing to the condition of the tracks of the Company, that the name of said Company became a terror to the traveling and shipping public, and a by-word and reproach. By means of said rails, the railways of the defendant were kept in safe running order, its business and importance increased, and the railway rendered more valuable to the bondholders under the various mortgages, and especially under the mortgage to be hereinafter referred to. The indebtedness for the rails was contracted by the Railway Company in consideration of its promise to pay for the same out of its earnings, and in the expectation and belief that they would be paid for out of the

said earnings; or if the earnings were insufficient, then out of the proceeds of sale of the property itself, by preference over mortgage creditors. The Railway Company, instead of paying the debt so due to petitioner, used a large amount of its earnings for the payment of coupons on bonds secured by its first mortgage.

The rails in question were furnished under two contracts:

(1) Under a contract of date April 26th, 1883, rails were delivered during the months of June, August and September, 1883, for which, pursuant to the terms of the contract, notes were issued in payment, and which were from time to time renewed after partial payments.

Of these rails, a portion was used upon the railways of the Waco and Northwestern Division of the Houston and Texas Central Railway, and upon that portion \$6426.51 remained due on the 16th day of February, 1885.

Certain bonds of the Galveston, Harrisburg and San Antonio Railway Company were pledged as security for this portion of the claim.

(2) Under the second contract, of date October 30th, 1883, rails were delivered during the months of February, March, April and May, 1884, the purchase price of which was evidenced by notes given under the terms of the contract, maturing six months from date of delivery, and which were, by the terms of the contract itself, subject to a right of renewal, which was exercised, so that the notes became due in February, March, April and May, 1885.

Of these rails, an amount worth at the contract price \$99,300.64, were laid upon the railways of the Waco and Northwestern Division. No security whatever was given under this contract.

Prior to the due date of any of the notes, due under the second contract, and to the due date of most of the notes due under the first contract, the railways of the Houston and Texas Central Railway Company, including the Waco and Northwestern Division, were placed in the hands of Receivers, and the railways of the Waco and Northwestern Division have there remained ever since. The Receivership has, however, undergone certain changes and modifications, and we shall now summarize the facts, in relation to such changes and modifications, and also state what net revenues accrued under each Receivership, as follows :

(a) Under a bill filed by the Southern Development Company, in February, 1885, Benjamin G. Clarke and Charles Dillingham were appointed Receivers on the 21st day of February, 1885. This was a bill filed by the Southern Development Company claiming a lien upon the net earnings of the Railway Company and all its property, superior in rank to the mortgage bonds, and was a bill to which mortgage trustees were defendants and not complainants. The bill was filed on behalf of the Southern Development Company in its own behalf and on behalf of all other persons similarly situated. The Lackawanna Company intervened and joined the Southern Development Company. This bill was dismissed on demurrer May 27th, 1886. This Receivership lasted until July 10th, 1886, and under it there was collected from the operations of the Houston and Texas Central Railway Company an amount of \$423,142.16 over and above operating expenses, taxes, etc.

(b) On July 10th, 1886, the old Receivership terminated and a new one was instituted, under which Charles

Dillingham, Nelson S. Easton and James Rintoul were appointed Receivers. This appointment was made in a suit known as Consolidated Cause No. 198, which was a cause wherein the trustees of mortgages upon the various divisions of the Houston and Texas Central Railway Company were complainants, and the Railway Company, itself, a defendant. The Farmers' Loan and Trust Company was a complainant, and filed a bill on behalf of other mortgages which it represented, but although the Court ordered it to stand as a complainant, in Cause No. 198, with leave to file a bill, *it never filed any bill or took any proceedings as trustee of the first mortgage on the Waco and Northwestern Division.* This Receivership lasted, in so far as the property of the whole system was concerned, up to some time subsequent to a sale of the property, and, say, up to some time in the spring of the year 1889, during which time these Receivers spent, outside of operating expenses, an amount of \$1,538,116.38, which, with the exception of a very small sum, either went to the mortgage creditors, or was expended in betterments on the property mortgaged.

In this Cause No. 198, the Lackawanna Company filed its petition of intervention, praying substantially for the same relief for which it prayed in suit No. 185, and for which it prayed in Cause No. 227, to be hereafter referred to.

(c) After the properties of the Houston and Texas Central Railway Company had been sold under final decree in Cause No. 198, in which decree the rights of the Lackawanna Company were expressly reserved for future adjudication, that Company filed its petition in Cause No.

198, asking that the Receivership therein should continue and remain over the property in possession of the Court until its claims should have been finally decreed and passed upon. At the same time the Farmers' Loan and Trust Company, appearing as trustee of the first mortgage of the Waco and Northwestern Division of the Houston and Texas Central Railway, filed its foreclosure bill, known as Bill No. 227, under which it obtained an order appointing a receiver of the Waco and Northwestern Division, who was the same receiver already in charge of the Houston and Texas Central lines. The filing of this bill April 6th, 1889, was the first attempt by the trustee to enforce its rights upon either *corpus* or income of the mortgaged property.

During the Receivership in Cause No. 198, interest was paid, by order of the Court, to holders of first mortgage bonds of the Waco and Northwestern Division, aggregating in amount \$91,371, under orders expressly rendered, "without prejudice to the rights of defendant or any intervenor in this cause, or any final decree to be rendered in the same, nothing herein being decided as to the merits of the claim of the defendants, or of intervenors, and this order not in any manner stopping or affecting the rights of any party or intervenors in this cause."

It is also shown that during the years 1883 and 1884, whilst the rails sold by the Lackawanna Company were being by it delivered to the Houston and Texas Central Railway Company, that Company paid out \$2,386,400 in interest on bonded indebtedness, whereof about \$1,300,000

was paid from income or current earnings, and out of which amount \$159,600 was paid as interest on the first mortgage bonds of the Waco and Northwestern Division. These interest payments were made out of the very monies which should have paid the Lackawanna claim.

Upon these facts we claim that the debt due the Lackawanna Company is clearly one entitled to an equitable lien upon earnings under the rule in *Fosdick vs. Schall*, and the other cases which followed that one.

In the brief which we filed in the Circuit Court of Appeals, and which is also filed here, the authorities are given at length; but the cases most similar to the one at bar are the cases of *Hale vs. Frost*, 99 U. S. 391, in which case Hale, Ayer & Company recovered upon a claim which extended back to a date long prior to *August, 1873*, for an amount which had been repeatedly evidenced by notes, upon which payments had been made and new notes given, and yet recovery was had in a Receivership instituted *May 19th, 1875*. And in *Burnham vs. Bowen*, 111 U. S. 777, the claim was for "monthly settlements of monthly accounts with a somewhat extended credit." In other words, just such a claim as that of the Lackawanna Company.

The only rule that we have been able to find, which has been sanctioned by your Honors is, that each case is to be decided upon its own merits, and that all claims of the nature allowed as liens enjoying priority over the mortgages must have been incurred within a reasonable time prior to the Receivership. Inasmuch as the allowance of a claim of the character of the one set up by the Lacka-

wanna Company is one resting so largely in the discretion of the Chancellor, it becomes important to show the nature of conflicting claims upon the revenues of the defendant Railway Company, because if no conflicting claims existed, or if the conflicting claims be of a character not commending themselves to the Chancellor, they may be disregarded in the exercise of the judicial discretion allowed in such cases.

That the mortgagees, under this mortgage, had no mortgage upon income, is seen from a mere inspection of their mortgage. (Rec. pp. 22 *et seq.*) Even if they had a mortgage upon income, such mortgage would have given them no lien upon the earnings of the road whilst it remained in the hands of the Company, nor until the trustee should take some steps, authorized by the mortgage, to appropriate the earnings. Especially is this the case where the effect of the mortgage of real property is not deemed a conveyance so as to enable the mortgagee to recover possession of the real property without a foreclosure and sale, according to law, and Texas is one of the States where it has been decided that a mortgage is a mere security for the payment of a debt, and that the mortgagee cannot sustain an action of ejectment against the mortgagor.

By the terms of the mortgage sued upon in this cause, the Railway Company was to remain in possession of its property, and had the right to operate the same and appropriate earnings and income until default, continuing for the time stipulated in the mortgage, in which event the trustee was empowered to take possession of the railroad

and operate it, applying net earnings to the satisfaction of interest. The trustee not only failed to take possession of the road, but never, until it filed its foreclosure bill in Cause No. 227, on the 6th day of April, 1889, took any steps whatsoever to assert any lien upon the earnings.

We therefore respectfully submit :

I.

That the claim of the Lackawanna Iron and Coal Company is one of the character repeatedly recognized by this Court as a charge in equity on the income of a railway company both prior to and during a receivership.

II.

That the Farmers' Loan and Trust Company, and the beneficiaries under its trust, had no lien upon any earnings of the Waco and Northwestern Division of the Houston and Texas Central Railway Company prior to April 6, 1889, and the Circuit Court having appropriated those earnings to payment of interest on the bonds represented by said Trust Company, as also to improving the property mortgaged, will now restore to the current income fund the amount diverted from it to the prejudice of current income creditors.

That we are not entirely alone in our belief that the judgment of the Circuit Court of Appeals is incorrect upon these questions will be seen from the following editorial notice of its decision in the *American Law Review*, for July and August, 1897, pages 611 and 612 :

“RAILROAD RECEIVERSHIPS: PREFERENTIAL DEBTS—WHEN PURCHASE OF RAILS NOT PREFERRED BEFORE LIEN OF PRIOR MORTGAGE.—In the case of *Lackawanna, etc., Co.*

vs. Farmers' Loan, etc., Co., lately decided in the Federal Circuit Court of Appeals for the Fifth Circuit, it is held that the purchase by a railroad company, under contracts made from about sixteen months to over two years before the appointment of a receiver, of some 20,000 tons of steel rails, to replace the old and deteriorated rails with which its tracks were laid, to be paid for by its notes, due in six months, renewable for six months longer at the railroad company's option, is not a purchase of supplies in the ordinary operation of the road to keep it a going concern, so as to authorize the court appointing the receiver to give the debt a preference over the mortgage debt. The Court of Appeals which decided this case consisted of three District Judges. The opinion of the court is written by Mr. District Judge Parlange. It reviews a good many of the decisions upon this subject, but not all of them. It is believed to be unsound. There is one case which has held the debt to partake of a preferential quality, although it is six years old." (*Union Trust Co. vs. Morrison*, 125 U. S. 591, 604). "Another gives it that quality where it was nearly five years old." (*Northern, etc., R. R. Co. vs. Lamont*, 69 Fed. Rep. 93). "If the reconstructing of a railroad track with steel rails so that it may be operated with safety to the public is not necessary to keep it a going concern, within the well-known rule upon this subject, what is?"

THE GROUNDS UPON WHICH THE WRIT OF CERTIORARI SHOULD ISSUE.

We respectfully submit that your Honors have never yet, in any case, directly passed upon the questions constituting the distinguishing features of this case, and controlling its correct decision.

Within a very few weeks from this date a cause will, in due course of judicial proceeding, be reached upon your calendar, wherein the full and exact scope and extent of the doctrine, announced in the case of *Fosdick vs. Schall*,

will be submitted to you for adjudication, in a case wherein you have heretofore issued a writ of *certiorari* to the Circuit Court of Appeals for the Fifth Circuit, to-wit., the case of *Rowena M. Clark et al. vs. The Central Railroad and Banking Company of Georgia et al.*, No. 100 of your Docket, for the October Term, 1897.

Your Honors have also granted a *certiorari* in the case entitled *Southern Railway Company vs. Carnegie Steel Company, Limited*, which cause is numbered 278 upon the Docket of this Court, for the October Term, 1897.

Not only will the whole doctrine, governing this cause, be the subject-matter of review and adjudication, in the two causes above-named, but in the last named case the Circuit Court of Appeals for the Fourth Circuit decided a cause which is, as to nearly every crucial fact, an exact duplicate of the cause now presented to your Honors in this petition, and which is its exact duplicate in law. The decision of the Fourth Circuit was in diametrical opposition to the decision in the Fifth Circuit.

The decision by this Honorable Court, in the case of the *Southern Railway Company vs. The Carnegie Steel Company, Limited*, will be absolutely decisive of this cause; provided the mandate of the Circuit Court of Appeals for the Fifth Circuit be stayed herein until the *Southern Railway Company* cause is reached by your Honors.

Under these circumstances, we respectfully submit that the importance of the questions involved in this cause, which are all questions of general jurisprudence; the fact that a similar cause has already been ordered to be certified by your Honors from another Circuit; the propriety of maintaining a uniformity of jurisprudence between differ-

ent Courts of Appeal; and the manifest hardship and wrong which will have been done to petitioners in this cause, if your Honors should leave them remediless and thereafter affirm the decision of the Circuit Court of Appeals for the Fourth Circuit, should be absolutely conclusive upon our right to the writ of *certiorari*. We have a right to have the decision in our cause stayed until this Honorable Court, which has become seized of all the questions of law, involved in it, shall have passed upon them, whether your decision be favorable or adverse to us.

Although we lay before you the full briefs submitted by us to the Circuit Court of Appeals, we, nevertheless, submit that your Honors will not, upon the present application, examine into, or decide either favorably or adversely to us, the questions involved in this case, and especially the one first stated above. You have, by granting the writ in the Southern Railway case, decided that that question is of such a nature that it should be reviewed by you. A decision, adverse to us upon this application, would, under the circumstances of this case, practically adjudicate questions of which you have taken jurisdiction, and upon which you will adjudicate only after full argument, and in due course of judicial proceedings. The identity of the issues, or of some of the issues, involved in this cause, with the issues, or with some of the issues, involved in the Southern Railway cause, being assumed and proved, the right to the writ of *certiorari* would seem to us to follow as a matter of course, reserving until a future time the correct exposition by this Court of the law applicable to this case.

No serious hardship can inure to the respondents, even if the final decision should be against us, for the reason

170. 451. No. 22

App^y to *Ex. of Kruttschnitt, The*
Jonas & Oakton for Per
Filed Dec. 11, 1897.

FILED
OCT 11 1897
JAMES H. MCKENNE

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1897.

No. 451.

THE LACKAWANNA IRON AND COAL COMPANY
ET AL., PETITIONERS,

versus

THE FARMERS' LOAN AND TRUST COMPANY
ET AL., RESPONDENTS.

COPY OF BRIEF FILED IN CIRCUIT COURT OF APPEALS, NOW
FILED IN SUPREME COURT IN SUPPORT OF APPLICA-
TION FOR WRIT OF CERTIORARI.

E. B. KRUTTSCHNITT,
E. H. FARRAR,
B. F. JONAS,
H. T. GURLEY,

*Solicitors and of Counsel for Lackawanna Iron and
Coal Co. and for Pacific Improvement Co.*

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UNITED STATES CIRCUIT COURT OF APPEALS

FIFTH CIRCUIT.

No. 503.

LACKAWANNA IRON AND COAL COMPANY Et
AL., APPELLANTS,

versus

FARMERS' LOAN AND TRUST COMPANY Et AL.,
APPELLEES.

On the 6th day of April, 1889, the Farmers' Loan and Trust Company, as complainant, filed a Bill of Complaint against the Houston and Texas Central Railway Company et als., seeking the foreclosure of a mortgage granted by the latter Company upon the division of its railways, known as the Waco and Northwestern Division. (Rec. pp. 8 *et seq.*)

In this proceeding the Lackawanna Iron and Coal Company filed a petition of intervention, the object of which petition was to obtain the recognition of an indebtedness due to it by the Houston and Texas Central Railway Company, which indebtedness had been represented by twenty-five promissory notes, maturing at different dates, in the first five months of the year 1885, and aggregating a total of \$445,175.50, and which indebtedness had been liquidated by a judgment of the District Court of Dallas

County, in the State of Texas, at the sum of \$555,914.25, with interest at eight per cent. per annum from May 17th, 1889.

These notes had been given in evidence of the purchase price of certain steel rails bought by the Houston and Texas Central Railway Company from the Lackawanna Iron and Coal Company, under circumstances described in the tenth paragraph of the petition (Rec. pp. 620-622), as follows :

"That all of said steel rails so delivered were used for the useful improvements and necessary repair of the main line of said Houston and Texas Central Railway Co., and of the western division thereof, and of the Waco and North-western division thereof, to the extent hereinafter more fully set forth. That said steel rails were so absolutely necessary to said Company to enable it to replace the old iron with which its tracks were laid, that it is doubtful whether said Company could have maintained its existence as a common carrier without them. That prior to the improvement and repair of said line of road with steel rails, as aforesaid, accidents to life and limb and damage to property was so great, owing to the condition of the tracks of said Company, that the name of the Houston and Texas Central Railway Company became a terror to the traveling and shipping public, and a by-word and reproach. That, by means of said steel rails so furnished by petitioner to said defendant railway, the railway of said defendant Company has been kept in safe running order, its business and importance increased, and said railway thereby rendered more valuable to the bondholders under the various mortgages thereupon, and especially to the bondholders under the deed of trust and mortgage held by complainant herein, and upon which its bill of foreclosure has been filed in this cause. That said indebtedness was contracted by defendant in consideration of its promise to pay the same out of the earnings of its railway. That your peti-

tioner made the contracts aforesaid, and furnished the steel rails aforesaid, under the expectation and belief that it would be paid for the same out of the revenues and earnings of said property; and that in case said revenues should not be sufficient, out of the proceeds of the sale thereof, by preference over any of the holders of mortgage bonds secured by deeds of trust on said property, but that said defendant, instead of paying the debt so justly due to your petitioner, out of the earnings of said railway, has entirely failed to pay the same, or any part thereof, as hereinabove set forth, and that the truth is, and your petitioner so charges, that the said defendant has used a large amount of said earnings for the payment of coupons upon bonds secured by the mortgage upon which a bill of foreclosure has herein been filed, although the holders of said coupons were only entitled to receive payment thereof after the defendant had paid your petitioner the amounts advanced and expended in the manner and for the purposes hereinabove set forth. That said steel rails so purchased by said Railway Company were actually used for the betterment and improvement of its railway aforesaid, and not for purposes of construction, and that the said rails have been an increment to the value of the property mortgaged to said bondholders, and that your petitioner has the right to claim and does claim that the revenues of said railway property should be applied to the payment of petitioner's said indebtedness, by preference over the claim of any bondholders or coupon holders, whomsoever."

The petition (R. pp. 623, *et seq.*) asked that an account might be taken, under the direction of the Court, as to the dates and amounts of money paid by the defendant Railway Company to any of the mortgagees in the various trust deeds, described in the petition, showing particularly the issue of bonds upon which such interest was paid; and what proportion of the amounts so paid were paid out of current revenues of the Company, in the absence of earn-

ings, and what amounts were so paid out of net earnings of the defendant Railway Company; and particularly so as to show what amounts and proportions were so paid out of the net earnings of those portions of the railway of the defendant Railway Company, described in the Bill of Complaint of the Farmers' Loan and Trust Company, hereinabove referred to; that an account might be taken showing the proportion of steel rails furnished by petitioner to the defendant Railway Company, used upon the railways described in the Bill of Complaint; and that the account to be taken should also show all receipts and expenditures made by the Receivers, in whose hands the property had been placed under proceedings which will be hereinafter at greater length detailed, and which account should be taken in such manner as to show the dates when the expenditures were made, and the character of the expenditures, and in such manner as to show whether the expenditures were made for operating and running expenses, or for extraordinary repairs, betterments and improvements of the property, and for the payment of fixed charges upon the same.

The petition further prayed that for the amounts due on such accounting to petitioner and equitably chargeable upon the railways described in the Bill of Complaint in said cause, there might be a decree against the defendant Railway Company, and against all of the parties complainant and defendant, decreeing the sum so due to be liens upon the net earnings of the Railway Company, and especially upon those portions of said net earnings which have accrued or may accrue from the railways described in the Bill of Complaint, both those accrued prior to the Receivership in

Cause No. 185, and those accrued and to accrue during the Receivership in Cause No. 198; and upon all of the property of the Railway Company, superior in rank to the claims of the trustee and of the holders of mortgage bonds and coupons issued under the deed of trust sought to be foreclosed by the Farmers' Loan and Trust Company; that the net earnings of the railway described in the Bill of Complaint should be first devoted to the payment of the accounts so decreed, and, if they should prove insufficient to pay the amounts, then that the Court should decree the payment of said amounts out of any proceeds of sale of the property of the defendant Railway Company to be made under final decree.

The Pacific Improvement Company, as assignee of the Lackawanna Company, was, by order of Court, and upon its petition, made a co-petitioner with the Lackawanna Company. (R. p. 646.)

This petition, with the answers of the Farmers' Loan and Trust Company, and of Moran Bros. et als., intervening bondholders (R. pp. 635 and 647), was referred to William L. Prather as a special master "to take the accounts prayed for, and to investigate, find and report upon the facts as to the subject matter of said petition, and of the answers thereto."

Under this petition facts were found, which will be found in the record, pp. 648 *et seq.*, from which we extract the crucial facts, and now state them as follows:

On the 28th day of December, 1882 (R. p. 650), the Lackawanna Iron and Coal Company entered into a written agreement with the Houston and Texas Central Railway Company, under which five thousand and twenty (5020) tons

of 56 lb steel rails were furnished to said Railway Company in the months of February, March, April and May, 1883, which rails were, in due course of time, paid for, and this contract is wholly immaterial to the issues before the Court, and is referred to merely as a fact in the history of this litigation, the non-statement of which might hereafter lead to some confusion.

On the 26th day of April, 1883, the said Lackawanna Company entered into another contract, in writing, with the Houston and Texas Central Railway Company, pursuant to which contract it delivered to said Railway Company five thousand and nine (5009) tons of 56 lb steel rails during the months of June, August and September, 1883, at the price of \$39.50 per ton. Pursuant to the terms of the contract, notes were issued in payment of these rails, aggregating in amount, with interest to their maturities, \$201,346.64; but which notes were from time to time renewed until they were reduced to eight in number, maturing at dates between January 20th, 1885, and April 24th, 1885, and aggregating in amount \$118,000. (R. pp. 651-2).

It is shown that 6.2 miles of the railway of the Waco and Northwestern Division of the Houston and Texas Central Railway were laid with rails furnished under the two contracts above described, but it was not shown what proportion of rails were furnished under each of the two contracts. (R. p. 655). As it is further shown that the Waco and Northwestern Division was run as a part of the system of railways belonging to the Houston and Texas Central Railway, and as it is impossible to separate the accounts of that division whilst it was in the possession of the Houston and Texas Central Railway from the accounts of the rest of the

system, it is only fair and equitable to assume that the rails furnished under the two contracts, which were about equal in amount, were divided about equally upon this 6.2 miles, which would give 3.1 miles laid with the rails furnished under the second contract.

The original contract price of the 5009 tons of rails was \$197,855.50, which was reduced by payments to \$118,000, as aforesaid. A simple calculation will show that upon 3.1 miles of road 272.8 tons of rail were required, because it requires 88 tons of 56 lb rails to lay one mile of road. (R. p. 655). And these rails, at the contract price of \$39.50 per ton, were worth \$10,775.60. If we pro-rate the payments made upon the contract, this indebtedness will be reduced to \$6,426.51, which represents the amount of rails furnished by the Lackawanna Company under the second contract to the defendant Railway Company, and used upon the roads of the Waco and Northwestern Division.

Under a third contract entered into between the Lackawanna Company and the defendant Railway Company on the 30th day of October, 1883, the Lackawanna Company delivered to the defendant Company 8552 tons of 54 lb steel rails during the months of February, March, April and May, 1884, the purchase price of which rails, evidenced by promissory notes maturing at different dates during the months of February, March, April and May, 1895, amounting to \$327,175.50. (R. pp. 653-4).

Of these rails it is shown that 30.8 miles were consumed upon the railways of the Waco and Northwestern Division of the Houston and Texas Central Railway. The contract price of the rails was \$36.60 per ton, and as it requires 84.86 tons of 54 pound rails to lay one mile of track, it fol-

lows that the value of the rails at the contract price was \$99,300.64. (R. pp. 655-6).

It therefore appears that there is still due upon the purchase price of rails furnished under the second contract, and laid upon the railways of the Waco and Northwestern Division of the Houston and Texas Central Railway a sum total of \$6426.61, and of the rails furnished under the third contract the whole purchase price is due, amounting, in so far as the Waco and Northwestern Division is concerned, to the sum of \$99,300.64 as aforesaid.

At the time when the Lackawanna Company made the contracts and furnished the rails in question, the condition of the track of the defendant Company was such that the demand for new rails upon the most worn portion of the same was practically imperative. For a number of years prior to December, 1882, only about 5000 tons of new rails had been purchased. The road north, from Houston, for 90 miles, was completed between 1857 and 1861, and thence northward to Denison between 1867 and 1872. The Waco Division was completed about 1875. The condition of the road was bad. There was continual breakage of rails and wreckage of trains; the track was unsafe, and was generally so regarded not only by railroad men, but by the traveling public; the damage to merchandise, rolling stock, etc., was continuous, and the need for new rails was absolutely necessary as a preservation of human life, the loss of which was liable to occur at any moment. Both buyer and seller expected the rails to be paid from the net income of the railway. The sale was made without any stipulation for security to be given by the defendant Com-

pany, or for payment out of any particular fund, or in any particular way. (R. pp. 656-7).

The rails supplied under these contracts were laid in the tracks of the defendant Railway Company as above stated. (R. p. 657). Within nine months after the last of these rails were delivered a Bill of Complaint was filed in the United States Circuit Court for the Eastern District of Texas by the Southern Development Company, praying, among other things, for the appointment of Receivers to the railways of the Houston and Texas Central Railway Company. (R. pp. 653 and 658).

Upon this bill, Benjamin G. Clarke and Charles Dillingham were appointed Receivers on the 21st day of February, 1885. This bill was filed by the Southern Development Company, seeking a marshaling of the assets of the defendant Corporation, and a declaration that its claim was secured by a lien upon the net earnings of the Railway Company, and upon all of its property, superior in rank to the mortgage bonds. This bill was filed by the Southern Development Company in its own behalf, and in behalf of all other persons similarly situated, who might intervene to protect their own interests. The Lackawanna Company did intervene, praying substantially for the same relief as is prayed for by its intervention in this cause. (Rec. pp. 659-668).

The Bill of Complaint of the Southern Development Company was, on the 27th day of May, 1886, dismissed upon demurrer, without prejudice to the rights of complainants to assert their claims, if any they had, in such manner as they might be advised; but prior to the dismissal of said bill, Nelson S. Easton, James Rintoul, and

Charles Dillingham were appointed Receivers of the properties of the defendant Railway Company, under three bills filed by various mortgage creditors, and which bills are generally known as Bills Nos. 198, 199 and 201 of the Chancery Docket of the Circuit Court of the United States for the Eastern District of Texas. (R. p. 662).

Clark and Dillingham, Receivers, turned over all the property in their possession to Easton, Rintoul and Dillingham, as Receivers, on the 10th of July, 1886, and these Receivers remained in possession of the property until December 7th, 1886, or thereabouts, when Easton and Rintoul were relieved from further duty, and Dillingham continued as sole Receiver. (R. 663).

The mortgages declared upon in the Causes Nos. 198, 199 and 201 were foreclosed by final decree entered in Consolidated Cause No. 198, under which number the three causes, together with others, had been consolidated, and under this decree all the property of the Railway Company was sold on the 8th of September, 1888, including the property of the Waco and Northwestern Division of the Houston and Texas Central Railway, which property, however, was sold subject to the mortgage forming the subject matter of the bill of foreclosure of the Farmers' Loan and Trust Company, filed under the No. 227 of the docket of the United States Circuit Court for the Eastern District of Texas, and subject, also, to the right which the Court reserved by its decree to charge upon the property, or any part thereof, the payment of any amount that might be found to be due and payable by reason of intervening petitions theretofore filed in said cause, and to be entitled to

priority over the mortgage debts referred to in the decree. (R. p. 663).

The Lackawanna Company filed its petition of intervention in said Cause No. 198, praying substantially for the same relief as it had prayed for in its petition in Cause No. 185, and praying substantially for the same relief as it prays for in its petition of intervention in Cause No. 227. (R. p. 616 *et seq.*)

Subsequently to the decree in said Cause No. 198 and to the sale made thereunder, the Lackawanna Company, on the 20th day of April, 1889, filed its petition in said Cause No. 198, asking that the Receivership therein should continue and remain over the property then in the possession of the Court, being the property now in the hands of the Receiver in this cause, until the claims and demands of the Lackawanna Company should have been finally decreed upon, and, if decreed in its favor, should have been finally paid and settled; and, further, praying the Court to render a preliminary order staying the order which had theretofore been rendered, directing the delivery of the property to one George E. Downs, who had become the purchaser thereof, and directing the Receivers not to deliver the property to any purchaser until after the final hearing of the matter of said petition. (R. p. 675).

On this petition an order was rendered directing Downs and the Farmers' Loan and Trust Company to show cause why the relief prayed for should not be granted; and further directing the Receiver to retain possession of the property until the further order of the Court; and further ordering that the Receivership which had theretofore been ordered in Cause No. 227 should be concurrent with the

original Receivership ordered in Cause No. 198, and that the Receiver should keep separate accounts of the earnings and expenses of the Waco and Northwestern Division of the Houston and Texas Central Railway Company. (R. p. 675).

It will thus be seen that ever since the Lackawanna Company filed its intervention in Cause No. 185, on the the 12th day of September, 1885, the Lackawanna Company has at all times had an intervention pending in the matter of the Receivership of the Waco and Northwestern Division of the Houston and Texas Central Railway Company in every phase which that litigation has assumed. It will be seen that the Receivership ordered in Cause No. 198 has been continued concurrently with the Receivership in Cause No. 227, down to the present day. Thus, any intimation of laches, or of sleeping upon rights, is conclusively disproved, in so far as the conduct of the Lackawanna Company, itself, is concerned.

It now behooves us to further show the conduct of the complainant, the Farmers' Loan and Trust Company, as Trustee of the first mortgage upon the Waco and Northwestern Division of the Houston and Texas Central Railway; to show the use made of the revenues of that division for the benefit of the first mortgage bondholders, and to show that in every order rendered in favor of those bondholders, they allowed a clause to be inserted providing that the order was rendered without prejudice to the rights of the defendant, or of any intervenor in the cause, and with express reservation of such rights.

We descend to particulars :

We have heretofore shown that the Southern Development Company filed its Bill in suit No. 185 of the docket of the United States Circuit Court for the Eastern District of Texas on the 16th day of February, 1885. It filed an Amended and Supplemental Bill, on the 20th day of February, 1885, after the appointment of Receivers. Prior to the filing of this Amended Bill, on March 31, 1885, the Farmers' Loan and Trust Company filed its petition in said Cause No. 185, praying to be made a party thereto, averring among other things that it was trustee under several different mortgages executed by the defendant Railway Company, and naming among others the mortgage sued upon in Cause No. 227. The prayer of the petition was granted on April 6, 1885; the Farmers' Loan and Trust Company was allowed to become a defendant in said suit No. 185, with a proviso that it might demur, plead or answer on or before the Rule Day in June, 1885. On June 15, 1885, pursuant to this leave, the Farmers' Loan and Trust Company answered both the Original and Supplemental Bill of the Complainant. An inspection of this answer will show, and the Master finds, that its averments are all defensive, and that this answer, with the petition praying to be made a party defendant, are the only pleadings and appearance made by the Farmers' Loan and Trust Company in Cause No. 185. and that it does not appear from said answer that the Farmers' Loan and Trust Company, as trustee for any of the mortgages mentioned in said answer, either demanded of the Court that the Receiver should hold the property for said trustee, or in any other manner demanded affirmative relief under any of

the mortgages under which it was a trustee. (R. pp. 671-2). Its appearance in said Cause No. 185 was simply that of a defendant, in opposition to the rights asserted in the original and supplemental bill of complaint.

We have already seen above that the bill in Cause No. 185 was dismissed upon demurrers, which demurrers were filed on October 5th, 1885, by Easton and Rintoul, Trustees, under different mortgages. This dismissal occurred May 27th, 1886 (R. p. 672); but on May 26th, 1886, prior to the entry of the order of dismissal, on motion of the defendant, the Houston and Texas Central Railway Company, an order was rendered in six causes, numbered respectively 183, 184, 188, 198, 199 and 201. This order was rendered upon consent of all parties in open Court. It first provided that no further proceedings should be had in Causes Nos. 183, 184 and 188, without notice to the defendant Railway Company. It further provided that Causes Nos. 198, 199 and 201 should be consolidated under the No. 198, and under the name and style of Nelson S. Easton and James Rintoul, Trustees, and the Farmers' Loan and Trust Company, Trustee, against the Houston and Texas Central Railway Company and Benjamin A. Shepard, Trustee, Consolidated Cause; that in said cause Easton and Rintoul should stand as complainants, as trustees under the mortgages or deeds of trust made by the defendant Railway Company, and bearing date respectively July 1st, 1886, and December 21st, 1870; that the Farmers' Loan and Trust Company, expressly assenting thereto, should stand as complainant under the mortgages or deeds of trust made by the defendant Railway Company, bearing dates respectively June 16th, 1873, October 1st, 1875, and April 1st, 1881, and that

Benjamin A. Shepard should stand as defendant, as trustee under the mortgage or deed of trust made by the defendant Railway Company, bearing date May 7th, 1877; that the bills filed in said Causes Nos. 198, 199 and 201 should stand as bills in the Consolidated Cause, and might be amended by either complainant, as they might be advised, by the August Rule Day, and that any party might file an answer to such original or amended bills as he might be advised within thirty days after said August Rule Day. No other action was taken in Causes Nos. 183, 184 and 188, after the order above mentioned, and it is unnecessary to further allude to them. Consolidated Cause No. 198 proceeded to final decree, and the three mortgages declared on therein were in all things foreclosed. (R. p. 673).

The Farmers' Loan and Trust Company, Trustee, in the mortgage declared upon in Cause No. 227, expressly assented to stand as complainant in said Cause No. 198, but filed no Bill of Complaint therein, and the Bill of Complaint in Cause No. 227 was not filed until long after final decree in Cause No. 198.

On March 21st, 1887, the Farmers' Loan and Trust Company filed an answer to the petition of Nelson S. Easton and James Rintoul in Cause No. 198, wherein and whereby the Farmers' Loan and Trust Company, as Trustee, under the Waco and Northwestern First Mortgage, being the mortgage forming the subject matter of the foreclosure proceedings now before this Court (under the No. 227), prayed the Court that any order which should be rendered in Cause No. 198, directing the payment by the Receivers out of the surplus of net earnings in their hands of any coupons falling due under any of the trust deeds by said

Railway Company, might order and provide for payment by the Receivers out of the surplus of net earnings in their hands of the two coupons due under the Waco and Northwestern Division first mortgage, as well as under the said other first mortgages. (R. p. 673).

The application of Easton and Rintoul, as also the application of the Farmers' Loan and Trust Company, for the payment of interest coupons, on the bonds secured by first mortgages or deeds of trust, described in the Bills of Complaint in said Consolidated Cause, came on to be heard on the 27th day of April, 1887, when an order was rendered by the United States Circuit Court for the Eastern District of Texas, that the coupons due January 1, 1885, and July 1, 1885, upon the first mortgage bonds of the Waco and Northwestern Division of the Houston and Texas Central Railway should be paid, with interest upon said coupons, due January 1, 1885, from January 1, 1885, until May 1, 1887, at the rate of six per cent. per annum, and with interest upon one-half of the coupon due July 1, 1885, from said last-named date until May 1, 1887, when the same was ordered to be paid, and upon the remaining one-half of said coupon until it should have been paid. The two coupons were paid pursuant to this order. The order expressly declared that it was :

"Without prejudice to the rights of defendant or any intervenor in this cause, or any final decree to be rendered in the same, nothing herein being decided as to the merits of the claim of the defendants, or of intervenors, and this order not in any manner stopping or affecting the rights of any party or intervenors in this cause."

The Farmers' Loan and Trust Company, as Trustee upon this same first mortgage of the Waco and Northwestern

Division, also filed petitions in the United States Circuit Court for the Eastern District of Texas, on the 6th day of November, 1888, and on the 20th day of November, 1888, for payment of the remaining coupon interest due upon the first mortgage of the Waco and Northwestern Division, upon which petitions no order was ever rendered.

By the final decree, rendered in Cause No. 198 on the 4th day of May, 1888, foreclosing the various mortgages sought to be foreclosed in said cause, the United States Circuit Court for the Eastern District of Texas expressly reserved the right to charge the property, under said decree ordered to be sold, with any amounts that it might decree in favor of any interventions then on file, and the intervention of the Lackawanna Company was on file at the time of said decree. (R. p. 674).

The amount of interest paid to holders of first mortgage bonds of the Waco and Northwestern Division, under the orders of Court above referred to, including the interest paid pursuant to said orders, amount to \$91,371. (R. p. 680).

This statement of facts is necessarily lengthy, and we now pause, in order to give a briefer and more condensed statement, to which we shall add a few other facts, not requiring any great space for their statement, nor any great amount of explanation.

1st. The Houston and Texas Central Railway Company owes the Lackawanna Iron and Coal Company the sum of \$6426.51, exclusive of interest and costs, for rails supplied by the Lackawanna Company to the Railway Company, under the second of the above described contracts, and used upon the Waco and Northwestern Division.

2d. The Houston and Texas Central Railway Company

owes the Lackawanna Iron and Coal Company the sum of \$99,300.64, contract price of rails furnished under the third of the above contracts to the Houston and Texas Central Railway Company, and used upon the Waco and North-western Division of that Company.

3d. These rails were furnished at a time when they were absolutely necessary, in order to maintain the existence of this portion of the system of the Houston and Texas Central Railway Company as a going concern; by their use the railway of the defendant Company was kept in safe running order, its business increased, and its railway thereby rendered more valuable to the bondholders under the various mortgages thereupon, and especially to the bondholders under the deed of trust and mortgage sought to be foreclosed in the proceedings now before the Court. The contracts were made, and the rails furnished under the expectation and belief that they would be paid for out of the revenues and earnings of the property, and if these were insufficient, out of the proceeds of sale thereof, but the defendant, instead of paying the debt due to the Lackawanna Company out of the said earnings, used the earnings for the purpose of paying coupons upon bonds secured by mortgage, upon which bonds the bill of foreclosure, now before the Court, was filed. The holders of these coupons were only entitled to receive payment after defendant had paid petitioner the amounts advanced and expended for the purchase of steel rails. The rails were actually used for the betterment and improvement of the railway, and not for the purposes of construction.

4th. Whilst the property of the defendant corpora-

tion was in the custody of the United States Circuit Court for the Eastern District of Texas, and before any proceedings whatsoever had been taken to impound the revenues of the defendant, or to affect them with any right whatsoever in favor of the bondholders, by order of said United States Circuit Court, an amount of \$91,371, out of the revenues of the railways of the Houston and Texas Central Railway Company, were paid to the holders of the bonds forming the subject matter of the foreclosure proceedings now before this Court for review.

5th. Whilst the property in question was thus in the custody of the United States Circuit Court for the Eastern District of Texas, its Receivers sold the rails removed from those portions of the Waco and Northwestern Division, upon which the new steel rails furnished by the intervening petitioner were laid; 2960 tons of such old rails were removed from the 37 miles laid with new steel rails, and were sold at a price of \$13 per ton net. This would give a salvage of \$32,032 from the sale of old material removed from the 30.8 miles of road, upon which new rails, furnished under the third contract, were laid, and \$3224 as the salvage through sale of old rails taken from the 3.1 miles laid with rails furnished under the second contract. (R. p. 656).

6th. During the years 1883 and 1884, whilst the rails in question were being furnished, the Houston and Texas Central Railway Company paid out \$2,386,400 in interest upon its bonded indebtedness, which amount, less \$1,043,198.27, which was borrowed for interest purposes, in those years, was presumably paid from income or current earnings. Out of this amount \$159,600 was paid as

interest on the first mortgage bonds of the Waco and Northwestern Division, being the bonds forming the subject matter of the Bill of Complaint in Cause No. 227. (R. p. 676).

7th. During the Receivership of Clarke and Dillingham, in Cause No. 185, they received from the operations of the railway of the defendant Company a total of. . \$4,902,218 45
 Their expenditures for operating expenses, taxes, etc., for the same period, amounted to. . . 3,479,076 29

Leaving a net balance from the operations of the railways of the Houston and Texas Central Railway Company, from February 23, 1885, to July 10, 1886, in cash, of. \$ 423,142 16

See figures (Rec. p. 666), which we have consolidated as above.

8th. Clarke and Dillingham collected from assets of the defendant Railroad Company, consisting of traffic balances, sales of old rails and old cars, a sum total of. \$265,921 42

(R. p. 667).

Easton, Rintoul and Dillingham, from the same source, collected 135,889 70
 (R. p. 668).

Total. \$401,811 12

9th. The Receivers, in Suits Nos. 185 and 198, Clarke, Dillingham, Easton and Rintoul, during their administration, expended a sum total of \$1,538,116.38 outside of operating expenses, all of which, except the sum of \$23,274.20, clearly went into the pockets of the mortgage creditors, or were expended in betterments upon the properties mortgaged

to them. In other words, a total of \$1,512,842.18 inured out of the revenues of the Receivership to the benefit of the mortgage creditors. (Rec. p. 667).

10th. The accounts of the defendant Railway Company were not kept in such a manner as to distinguish between earnings and expenses on the Waco and Northwestern Division, and those derived from the other divisions of defendant Company's Railway. (Rec. p. 680).

11th. The properties mortgaged to the Farmers' Loan and Trust Company, under the mortgages sought to be foreclosed in this cause, were the lines of the Houston and Texas Central Railway from Bremond to Ross, commonly known as the Waco and Northwestern Division, extending a distance of fifty-eight miles, whilst all the roads of the defendant corporation, including the Waco and Northwestern Division amount to a total mileage of 521 $\frac{1}{4}$ miles. (Bill of Complaint, R. p. 9). In other words, the Waco and Northwestern Division constitutes 11 13-100 per cent. of the whole system.

12th. The indebtedness due by the Houston and Texas Central Railway Company to the Lackawanna Company was liquidated by judgment of the District Court of Dallas County, in suit instituted by the Lackawanna Company against the defendant Railway Company, at the sum of \$555,914.25, with interest at eight per cent. per annum from May 17th, 1889 (R. p. 676), and upon this judgment execution issued August 19th, 1889, which was returned by the Sheriff of Dallas County not executed, there being no property found in Dallas County, subject to execution. (R. p. 670).

Upon these facts, the intervention of the Lackawanna

Iron and Coal Company came to trial before the Honorable the United States Circuit Court for the Eastern District of Texas, which Court dismissed the same.

The cause is brought into this Court by an appeal under which error has been assigned as follows :

First. The said decree is erroneous in denying the relief herein prayed for by intervenors and in dismissing the intervention herein.

Second. That the claim of intervenors is one made for materials and supplies necessary to keep the railways forming the subject matter of the foreclosure herein a going concern from day to day. That a continuance of the running of said railway involved the interests of the public, the traffic of the road and the continuance of the franchises of the defendant Railway Company herein, and that said supplies, added to the value of the property mortgaged to complainant herein, and the debt incurred for the same was and is entitled to preference both upon the revenues of the railways forming the subject matter of this cause, and upon the *corpus* of the same, over the claims of complainant herein, and that this Honorable Court erred in not so holding, and in not decreeing in favor of intervenors as in their intervention prayed for.

Third. That the income of the railways forming the subject matter of the bill of foreclosure in this cause, both prior to the filing of complainant's bill of foreclosure herein and subsequent thereto, and both prior to and subsequent to the taking possession of said railways by this Honorable Court, was used for the payment of interest upon complainant's mortgage and for permanent improvements upon said railways, and was diverted for the benefit of complainant herein

and of the holders of bonds described in the mortgage forming the subject matter of the bill of foreclosure herein, and at the expense of the current debt fund, and that intervenors are entitled to a restoration to the extent of such diversion of said current debt fund, and that this Honorable Court erred in not decreeing such restoration, and in not decreeing in favor of intervenors upon the current debt fund when thus restored.

Fourth. That the debt of intervenors is entitled to a lien upon the revenues of the defendant Railway Company in the possession of this Honorable Court, both under the laws of the State of Texas and under general principles of equity jurisprudence, and that both under said laws and under said jurisprudence intervenors are entitled to a payment of their claim out of said revenues, with priority over the claim of complainant herein, and that this Honorable Court erred in not so holding and ordering. (R. pp. 683, 684).

Instead of following the assignment of errors closely, we think that we can present the case more satisfactorily to the Court by discussing it in the manner in which we shall, and if that discussion proves satisfactory to your Honors, it will necessitate the sustaining of these assignments of error, and the rendering of a decree in favor of the Lackawanna Iron and Coal Company, intervenor.

We maintain, and shall press upon your Honors the following propositions, to-wit.:

I.

That the claim of the Lackawanna Company is one of the character repeatedly recognized by the Supreme Court of the United States as a charge in equity on the continuing

income of a railway company as well that which comes into the hands of the Court after the receiver is appointed as that before, and that so far as this current expense creditor is concerned, the Court should use the income of the receivership in the way in which the company would have been bound in equity and good conscience to use it, if no change in the possession had taken place; and further, that if the income has been diverted from the payment of current income creditors to the payment of mortgage creditors, or to the improvement of the mortgaged property, the current income fund, to the extent to which it has been depleted, will be restored out of the proceeds of sale of the mortgaged property.

II.

That the Farmers' Loan and Trust Company and the beneficiaries under its trust have never had a lien upon any of the earnings of the Waco and Northwestern Division of the Houston and Texas Central Railway Company, and they have no lien upon any such income now in the hands of the Court.

III.

If neither party has, nor at any time during this litigation has had, a lien on the income of the railways mortgaged in this case, then the Court will proceed upon the principle that equality is equity, and will distribute the income ratably among all the creditors of the defendant Railway Company before the Court.

I and II.

The authorities upon the first two propositions are, in many instances, the same cases, and we therefore consider them together, and we say that a long line of authorities,

beginning with the case of *Fosdick vs. Schall*, 99 U. S. 235, and running down to the present day, maintain the propositions :

1st. That a mortgagee, even where the income is mortgaged, has no lien upon the earnings of a railway company while the property remains in the hands of the company, nor until the mortgagee takes some steps authorized by the mortgage or by the course of equity procedure to appropriate the earnings.

2d. That even where income is mortgaged, the income out of which the mortgagee is entitled to be paid while out of possession, is the net income obtained by deducting from the gross earnings what is required for necessary operating and managing expenses, proper equipments and useful improvements. From this it follows, that persons to whom debts are due at the time a mortgaged road goes into the hands of a receiver, for necessary operating and managing expenses, proper equipments, and useful improvements, are entitled to a priority over mortgage creditors as to any fund derived from income which may be received by the receiver from the company.

3d. That an unpaid creditor, for necessary operating and managing expenses, proper equipments and useful improvements, is entitled to priority over mortgage creditors as to any fund derived from income whilst the property is in the hands of a receiver of the Court.

4th. That where current earnings have been used by the officers of a company, or by the Court, for the benefit of mortgage creditors, in paying bonded interest, purchasing additional equipments, or making permanent improvements on the fixed property, the mortgage security is

chargeable in equity with the restoration of the fund thus improperly diverted.

5th. If the current earnings claimant has been guilty of laches, no preference will be allowed to him over the mortgage creditor. It is difficult, if not impossible, to lay down any fixed rule or rules as to when claims should be considered stale. Each case must be governed by the particular facts which appear therein. The limit of six months, sometimes referred to, is not supported by the slightest authority, in so far as the decisions of the Supreme Court are concerned.

We now turn to the authorities :

In the 99 *U. S.* are found the four cases of *Fosdick vs. Schall*, p. 235; *Fosdick vs. Car Company*, p. 256; *Huidekoper vs. Locomotive Works*, p. 258, and *Hale vs. Frost*, p. 389.

The first of these is the leading case upon the relative rights of secured and unsecured creditors of railroads which have been placed in the hands of receivers. The other three cases are mere applications of the doctrine laid down in the first case, which was exhaustively argued, and wherein the Supreme Court of the United States arrived at a conclusion which has ever since been the law of the Federal Courts.

The decision is one which it is very difficult to condense, for the reason that it is a leading case upon a most important subject, and the quotations which we shall now make from it are unsatisfactory, at best. The exact question which drew from the Court the expressions which we shall quote, was this: "Was the order for the payment out of the fund in Court of the rent of certain cars during the time that they were used by the receivers appointed by the

State Court, and for six months before, justifiable under the circumstances of the case?"

The receivership in the case before the Supreme Court had been instituted in a State Court, but the cause was subsequently removed to the United States Circuit Court, so that, for all practical purposes, the case was the same as if it had been originally instituted in the Circuit Court.

Answering the above question, the Court said (*99 U. S. pp. 251 et seq.*):

"As to the second question, we have no doubt that when a court of chancery is asked by railroad mortgagees to appoint a receiver of railroad property, pending proceedings for foreclosure, the court, in the exercise of a sound judicial discretion, may, as a condition of issuing the necessary order, impose such terms in reference to the payment from the income during the receivership of outstanding debts for labor, supplies, equipment, or permanent improvement of the mortgaged property as may, under the circumstances of the particular case, appear to be reasonable. Railroad mortgages and the rights of railroad mortgagees are comparatively new in the history of judicial proceedings. They are peculiar in their character and affect peculiar interests. The amounts involved are generally large, and the rights of the parties oftentimes complicated and conflicting. It rarely happens that a foreclosure is carried through to the end without some concessions by some parties from their strict legal rights, in order to secure advantages that could not otherwise be attained, and which it is supposed will operate for the general good of all who are interested. This results almost as a matter of necessity from the peculiar circumstances which surround such litigation.

"The business of all railroad companies is done to a greater or less extent on credit. This credit is longer or shorter, as the necessities of the case require; and when companies become pecuniarily embarrassed, it frequently

happens that debts for labor, supplies, equipment and improvements are permitted to accumulate, in order that bonded interest may be paid and a disastrous foreclosure postponed, if not altogether avoided. In this way the daily and monthly earnings which ordinarily should go to pay the daily and monthly expenses are kept from those to whom in equity they belong, and used to pay the mortgage debt. The income out of which the mortgagee is to be paid is the net income obtained by deducting from the gross earnings what is required for necessary operating and managing expenses, proper equipment, and useful improvements. Every railroad mortgagee in accepting his security impliedly agrees that the current debts made in the ordinary course of business shall be paid from the current receipts before he has any claim upon the income. If for the convenience of the moment something is taken from what may not improperly be called the current debt fund, and put into that which belongs to the mortgage creditors, it certainly is not inequitable for the court, when asked by the mortgagees, to take possession of the future income and hold it for their benefit, to require as a condition of such an order that what is due from the earnings to the current debt shall be paid by the court from the future current receipts before anything derived from that source goes to the mortgagees. In this way the court will only do what if a receiver should not be appointed the company ought itself to do. For even though the mortgage may in terms give a lien upon the profits and income, until possession of the mortgaged premises is actually taken or something equivalent done, the whole earnings belong to the company and are subject to its control. *Galveston Railroad vs. Cowdrey*, 11 Wall. 459; *Gilman et al. vs. Illinois and Mississippi Telegraph Co.*, 91 U. S. 603; *American Bridge Co. vs. Heidelberg*, 94 Id. 798.

"The mortgagee has his strict rights which he may enforce in the ordinary way. If he asks no favors, he need grant none. But if he calls upon a court of chancery to put forth its extraordinary powers and grant him purely equitable relief, he may with propriety be required to

submit to the operation of a rule which always applies in such cases, and do equity in order to get equity. The appointment of a receiver is not a matter of strict right. Such an application always calls for the exercise of judicial discretion; and the Chancellor should so mould his order that, while favoring one, injustice is not done to another. If this cannot be accomplished, the application should ordinarily be denied.

"We think, also, that if no such order is made when the receiver is appointed, and it appears in the progress of the cause that bonded interest has been paid, additional equipment provided, or lasting and valuable improvements made out of earnings which ought in equity to have been employed to keep down debts for labor, supplies and the like, it is within the power of the court to use the income of the receivership to discharge obligations which, but for the diversion of funds, would have been paid in the ordinary course of business. This, not because the creditors to whom such debts are due have in law a lien upon the mortgaged property or the income, but because, in a sense, the officers of the company are trustees of the earnings for the benefit of the different classes of creditors and the stockholders; and if they give to one class of creditors that which properly belongs to another, the court may, upon an adjustment of the accounts, so use the income which comes into its own hands, as if practicable, to restore the parties to their original equitable rights. While, ordinarily, this power is confined to the appropriation of the income of the receivership and the proceeds of moneyed assets that have been taken from the company, cases may arise where equity will require the use of the proceeds of the sale of the mortgaged property in the same way. Thus it often happens that, in the course of the administration of the cause, the court is called upon to take income, which would otherwise be applied to the payment of old debts, for current expenses, and use it to make permanent improvements on the fixed property, or to buy additional equipment. In this way the value of the mortgaged property is not unfrequently materially increased.

It is not to be supposed that any such use of the income will be directed by the court, without giving the parties in interest an opportunity to be heard against it. Generally, as we know, both from observation and experience, all such orders are made at the request of the parties or with their consent. Under such circumstances, it is easy to see that there may sometimes be a propriety in paying back to the income from the proceeds of the sale what is thus again diverted from the current debt fund in order to increase the value of the property sold. The same may sometimes be true in respect to expenditures before the receivership. No fixed and inflexible rule can be laid down for the government of the courts in all cases. Each case will necessarily have its own peculiarities, which must to a greater or less extent influence the Chancellor when he comes to act. The power rests upon the fact, that in the administration of the affairs of the company the mortgage creditors have got possession of that which in equity belonged to the whole or a part of the general creditors. Whatever is done, therefore, must be with a view to a restoration by the mortgage creditors of that which they have thus inequitably obtained. It follows that if there has been in reality no diversion, there can be no restoration; and that the amount of restoration should be made to depend upon the amount of the diversion. If in the exercise of this power errors are committed, they, like others, are open to correction on appeal. All depends upon a proper application of well settled rules of equity jurisprudence to the facts of the case, as established by the evidence."

The other most important case to which we shall direct the attention of the Court is the case of *Burnham vs. Bowen*, 111 U. S. 777 et seq.:

"When a court of chancery, in enforcing the rights of mortgage creditors, takes possession of a mortgaged railroad and thus deprives the company of the power of receiving any further earnings, it ought to do what the company would have been bound to do if it had remained in

possession, that is to say, pay out of what it receives from earnings all the debts which in equity and good conscience, considering the character of the business, are chargeable upon such earnings. In other words, what may properly be termed the debts of the income should be paid from the income, before it is applied in any way to the use of the mortgagees. The business of a railroad should be treated by a court of equity under such circumstances as a 'going concern,' not to be embarrassed by any unnecessary interference with the relations of those who are engaged in or affected by it."

* * * * *

"Under these circumstances, we think the debt was a charge in equity, on the continuing income, as well that which came into the hands of the court after the receiver was appointed as that before. When, therefore, the court took the earnings of the receivership and applied them to the payment of the fixed charges on the railroad structures, thus increasing the security of the bondholders at the expense of the labor and supply creditors, there was such a diversion of what is denominated in *Fosdick vs. Schall* the 'current debt fund,' as to make it proper to require the mortgagees to pay it back. So far as current expense creditors are concerned, the court should use the income of the receivership in the way the company would have been bound in equity and good conscience to use it if no change in the possession had been made. This rule is in strict accordance with the decision in *Fosdick vs. Schall*, which we see no reason to modify in any particular."

* * * * *

"We do not now hold, any more than we did in *Fosdick vs. Schall*, or *Huidekoper vs. Locomotive Works*, 99 U. S. 258-260, that the income of a railroad in the hands of a receiver, for the benefit of mortgage creditors who have a lien upon it under their mortgage, can be taken away from them and used to pay the general creditors of the road. All we then decided, and we now decide, is, that if current earnings are used for the benefit of mortgage creditors before current expenses are paid, the mortgage security

is chargeable in equity with the restoration of the fund which has been thus improperly applied to their use. The decree of the Circuit Court is affirmed."

There does not seem to be much contest as to these general principles, but there is a vague claim that the intervenor has been guilty of some ill-defined laches, and an attempt is made to insist upon the "six months" rule, which has been recognized in some cases by inferior Federal Courts.

The Supreme Court is sometimes said to have laid down the six months rule in the case of *Fosdick vs. Schall*, but this is clearly a mistake.

The decree in the lower court was in favor of Schall, allowing him the rental of the cars for six months before the appointment of the receiver. This portion of the decree was reversed in the Supreme Court, because it was held that Schall had no contract of lease, and was, therefore, entitled to no rental, and no question ever arose requiring the Supreme Court to fix a limit prior to the receivership, beyond which it would not go in paying current earning creditors.

In *Hale vs. Frost*, however, in the same volume, the facts were that the receiver was appointed *May 19th, 1875*, and that Hale, Ayer & Company recovered upon a claim which extended back to a date long prior to *August, 1873*, and for an account which had been repeatedly evidenced by notes, upon which payments had been made, and new notes given. (*See 99 U. S. 391*).

In the case of *Burnham vs. Bowen*, the claim allowed was for coal furnished during the year 1874, but the precise time was not given. The receiver was appointed in Janu-

ary, 1875, and the claim was allowed, Chief Justice Waite saying:

"In the agreed facts upon which the case was heard below, it is stated that the coal was furnished during the year 1874, but the precise time in the year is not given. From what does appear, however, we are satisfied that at the time of the appointment of the receiver this was one of the current debts for operating expenses, made in the ordinary course of continuing business, to be paid out of current earnings, and that the payment would have been made at the time agreed on if the company had remained in possession. The renewed acceptances given after the receiver was appointed, indicate that the originals were for different amounts, maturing a month apart, thus implying monthly settlements of monthly accounts of a somewhat extended credit to meet the business requirements of what may have been, and probably was, at the time, an embarrassed railroad company."

Read the Master's Report; look at the list of notes contained at page 676, and you will see a duplicate of the case of *Burnham vs. Bowen*.

We do not think it necessary to give extended citations from any other authorities at the present time, but would merely refer to the case of *Union Trust Company vs. Illinois Midland Railway Co.*, 117 U. S. 434, which fully affirmed everything held in the foregoing cases, and which is also of importance upon other matters to which we shall hereafter have occasion to refer.

We would also refer to the case of *Union Trust Company vs. Morrison*, 125 U. S. 613, in which case the Supreme Court held, in reference to cases of this class, that each case was one *sui generis*; and in reference to the special case at bar, said:

"The case is a special one ; and in view of the discretion which the Court of first instance is obliged to exercise in matters of this character, taking all the circumstances into consideration, we cannot say that equitable relief was unduly extended in allowing the intervenor's claim."

The only rule, so far as we have been able to find, which has been sanctioned by the Supreme Court of the United States, is, that each case is to be decided upon its own merits, and that all claims of the nature allowed as liens enjoying priority over mortgages, must have been incurred within a reasonable time prior to the receivership. What is a reasonable time is a question of law, depending upon all the circumstances of the particular case. See *Paine vs. Central Vermont Railroad Company*, and cases cited, 118 U. S. 160.

That a first mortgagee who is made a party to a suit filed by a junior encumbrancer, wherein a receiver is appointed, who stands by and allows the income of the mortgaged property to be used in making betterments upon the property, is estopped from afterwards objecting to a decree restoring to the current debt fund income, thus diverted and used for improving the security of the mortgage creditor, is distinctly held in *Milttenberger vs. Logansport R. R. Co.*, 106 U. S. 286; *Union Trust Company vs. Illinois Midland Ry. Co.*, 117 U. S. 434, and *Souther vs. Railroad Co.*, 107 U. S. 591.

In the latter case, Chief Justice Waite said :

"The income of the receivership, instead of being applied in accordance with the order to pay the debts for supplies and labor, was used, with the consent, and it may fairly well be inferred, at the request of the bondholders, to buy additional grounds, rolling stock, etc., and to make permanent improvements, thus adding to the value of the

property which was afterwards sold. There is nothing whatever to indicate that in thus using the income, it was the intention of the Court to revoke the original order. It seems to have been found, in the administration of the cause, that by using the income to add to the value of the fixed property, the interests of all parties would be promoted, and so the fund which in equity belonged to the labor and supply creditors, was for the time being diverted from them and put into improvements and additions, the proceeds of which are now in Court. It is not to be presumed that this diversion would have been authorized if the value of the property added to and improved was not to be correspondingly increased.

"Clearly, therefore, on the face of the transaction, the fund in Court represents in equity the income which belongs to the labor and supply creditors, as well as the mortgage security, and there was no impropriety in appropriating it, as far as necessary to pay the creditors specially provided for when the receiver was appointed."

The case of the *Union Trust Co. vs. Illinois Midland Ry. Co.*, 117 U. S. 434, is also authority for the proposition that it is proper to apportion among the several sections of a railway in proportion to their length, the items allowed priority of lien. The Court rests its conclusion upon a number of considerations, and the whole argument upon the subject, and the decision of the Court upon this particular branch of the case, will be found at pages 465 to 469, inclusive, of the volume referred to.

The most important portion of the decision, and the one particularly applying to this case, is stated as follows by Judge Blatchford, on page 468 :

"Independently of this, it is entirely sufficient to rest our conclusion on the principle that non-action on the part of the Paris and Decatur bondholders and their trustee, which allowed the court and the receivers to go on during the en-

tire litigation, contracting debts in respect to the whole line operated as a unit, and administering the property as one, under circumstances where, as shown, it was and is impossible to separate the interests as to expenditures and benefits, in respect to the matters now questioned, and where important rights have accrued on the faith of the unity of the interests, amounts to such acquiescence as should operate as an estoppel. The interlocutory decree contains a clause in accordance with the foregoing conclusion, and, for the reasons above stated, we think it is right."

From an application of the principles of the above decisions to the facts of this case, we respectfully submit that the following conclusions are sound, to-wit:

1st. The Lackawanna Iron and Coal Company is a current earnings creditor, within the meaning of the doctrine in *Fosdick vs. Schall*, and the other cases following that case.

2d. The Lackawanna Company by reason of the saving clauses contained in every decree and order rendered by the United States Circuit Court for the Eastern District of Texas, affecting the income of the railways in its possession, up to and including the foreclosure decree in No. 227, stands to-day in the same position that it did on the day on which it filed its original intervention in suit No. 185.

3d. The Farmers' Loan and Trust Company and the beneficiaries under its trust, under the clauses in these same decrees and orders, taken or accepted by them without protest, are now estopped from denying that the Lackawanna Company stands exactly where it stood when it filed its intervention in Cause No. 185. The Lackawanna Company is entitled to a decree recognizing its lien for the sum of \$6,426.51 and \$99,300.64, being the proportionate price of rails laid upon the Waco and Northwestern

Division, and these amounts bear interest at 6 per cent. per annum from May 21, 1885, until paid, this being the due date of the last of the notes given to the Lackawanna Company, and being adopted as the date most favorable to the Farmers' Loan and Trust Company, and in order to avoid an intricate calculation apportioning the amount due in respect to the Waco and Northwestern Division to each of the many notes given to the Lackawanna Company.

4th. The decree in favor of the Lackawanna Company is justified upon every principle laid down by the Supreme Court as to the rights of a current income creditor as against a mortgagee of the income; and *a fortiori* against a mortgagee who, like the Farmers' Loan and Trust Company, in this case, has no mortgage of the income.

5th. It is shown that the Receivers in Cause No. 185 collected from the operations of the railways of the defendant Railway Company, during their administration, \$423,000 over and above all their expenditures of every kind whatsoever; also, that they collected from assets of the defendant Railroad Company, consisting of traffic balances, sales of old rails and old cars, a sum total of \$401,811.12. It is shown further, that the said Receivers expended a sum total of \$1,512,842.18 out of the revenues of the Receivership for the benefit of mortgage creditors. As the mileage of the Waco and Northwestern Division constituted 11.13 per cent. of the mileage of the whole Houston and Texas Central system, it follows that the *pro rata* of such expenditures to be charged to the Waco and Northwestern Division amounts to \$168,379.33, whereof \$91,300 was paid to the mortgage creditors for coupons upon their bonds, and the remainder expended in betterments, fully described in

the Master's findings. The diversion was therefore ample to cover our claim in full, with interest.

Against all the decisions which we have cited, the counsel for the intervenors, Moran Bros. and others, cites the case of *Bound vs. South Carolina Railway Company*, a decision rendered by Judge Fuller and Judges Hughes and Morris in the Circuit Court of Appeals for the Fourth Circuit, reported in *58 Fed. Rep. 473*, reversing the well considered opinion of Judge Simonton, which will be found in *47 Fed. Rep. p. 30*.

Whether or not the extreme necessity for the rails was shown in the Bound case that has been shown in this case, does not appear from the report, but, however that may be, we respectfully submit that the decision in question is at variance with the whole line of decisions which we have cited, and should be disregarded. We ask this Court to follow the long line of decisions of the Supreme Court, rather than a single contradictory decision of another Court of concurrent jurisdiction with yourselves.

Inasmuch as the allowance of a claim of the character of the one set up by the Lackawanna Company is one resting so largely in the discretion of the Chancellor, it is important to show the nature of any conflicting claims upon the revenues of the defendant Railway Company, because if no conflicting claims exist, or if the conflicting claims be of a character not commending themselves to the Chancellor, they may be disregarded in the exercise of the judicial discretion allowed in such cases. That the mortgagees, under this mortgage, had no mortgage upon income, is seen from a mere inspection of their mortgage. Even if they had had a mortgage upon income,

such mortgage would have given them no lien upon the earnings of the road while it remained in the hands of the Company.

Railroad Co. vs. Cowdry, 11 Wall. 483.

Smith vs. Railroad, 124 Mass. 157.

Gilman vs. Telegraph Company, 91 U. S. 616.

Bridge Co. vs. Heidelberg, 94 U. S. 798.

The lien of a mortgage upon the earnings of a railroad depends solely upon its terms, and until the trustee takes some steps authorized by the mortgage to appropriate the earnings, no lien attaches to them. *Miltenberger vs. Logansport Railway Co.*, 106 U. S. 307.

Another most instructive case upon this branch of the subject is *Kountze vs. Omaha Hotel Company*, 107 U. S. 378, *et seq.*

This case was an action on an appeal bond given for *supersedeas* of execution on a decree of foreclosure rendered by the Circuit Court for the District of Nebraska, and the question was as to the measure of damages to be recovered on the bond. In determining this question it was necessary to determine whether or not the plaintiffs were entitled to recover rents and profits or damages for the use and detention, as it is otherwise called.

Upon this branch of the case Judge Bradley, in 107 U. S. 392 *et seq.*, said :

"And yet there is a material difference between the case of ejectment and a suit for the foreclosure of a mortgage.

"The difference is this : In ejectment the property of the land is in question, and if the plaintiff has the right, he is entitled to immediate possession, and to the perception of the rents and profits, which belong to him, and for which the defendant in possession is accountable to him.

Every dollar, or dollar's worth, is so much of the plaintiff's property of which he is deprived. And the same is true in dower. But, in the case of a mortgage, the land is in the nature of a pledge; and it is only the land itself—the specific thing—which is pledged. The rents and profits are not pledged; they belong to the tenant in possession, whether the mortgagor or a third person claiming under him. This is not only the common law, but it is the express statute law of Nebraska, which declares that, 'in the absence of stipulations to the contrary, the mortgagor retains the legal title and right of possession.' The plaintiff in this case was not entitled to possession, nor to the rents and profits. His foreclosure suit did not seek possession, but sought a sale of the specific thing—the land. In such a case, until the litigation is ended, it doth not appear that there must be a sale, or even that the plaintiff is entitled to a sale. The defendant in possession is entitled to redeem the land until a sale is made, and until then he is entitled to the rents and profits which belong to him as of right. The taking of the rents and profits prior to the sale does not injure the mortgagee, for the simple reason that they do not belong to him. Waste, that is, destruction or injury to the land itself, as before stated, is an injury to the mortgagee. It diminishes the value of the pledge; and for such injury no doubt he might recover on an appeal bond. Other deteriorations, such as occur by want of repairs, accumulation of taxes, fires not covered by reasonable insurance, and the like, probably might also be fairly covered by the bond. But perception of rents and profits is the mortgagor's right until a final determination of the right to sell, and a sale made accordingly."

See also *Teal vs. Walker*, 111 U. S. 242, where the Court, after announcing the general doctrine, further holds, that the case against the right of the mortgagee to recover rents and profits before foreclosure, is strengthened by the provisions of the General Statutes of the State of Oregon, to the effect that a mortgage of real property shall not be

deemed a conveyance so as to enable the owner of the mortgage to recover possession of the real property without a foreclosure and sale according to law.

The laws of Texas are exactly the same upon this subject as those of the State of Oregon.

Article 1340 of the Revised Statutes of Texas (see 1 Sayles Texas Civil Statutes, p. 447) provides that:

"Judgments for the foreclosure of mortgages and other liens shall be, that the plaintiff recover his debt, damages and costs, with a foreclosure of the plaintiff's lien on the property subject thereto, and that an order of sale shall issue to the sheriff or any constable of the county where such property may be, directing him to seize and sell the same as under execution, in satisfaction of the judgment, etc."

The Supreme Court of Texas, by a long line of decisions, the most noteworthy of which is the case of *Duty vs. Graham*, 12 Texas, 427, has expressly decided that, under this statute, and under the laws of the State of Texas, a mortgage is a mere security for the payment of a debt. The mortgagor remains the real owner of the land and entitled to its possession, and the mortgagee cannot sustain an action of trespass to try title or ejectment against the mortgagor on the mortgage.

By the terms of the mortgage sued upon in this cause, the Houston and Texas Central Railway Company was to remain in possession of its property, and had the right to operate the same and appropriate earnings and income until default, continuing for the time stipulated in the mortgage, in which event the trustee was empowered to take possession of the railroad and operate it, applying net earnings to the satisfaction of interest. The trustee not

only failed to take possession of the road, but never, until it filed its foreclosure bill in Cause No. 227, took any steps whatsoever to assert any lien upon the earnings.

The provision of the mortgage, that the trustee should take possession, is, however, absolutely worthless, under the laws of the State of Texas.

We, therefore, respectfully submit that the Farmers' Loan and Trust Company has never had the slightest title to the rents and revenues of the property of the defendant corporation, either before or since the filing of its bill of foreclosure in this cause, and we, therefore, conclude that the Lackawanna Company and others similarly situated are the only persons before the Court having any claim to the income in question.

We do not particularly refer to the claims of the defendant, Downs, for the reason that he bought under the terms of a final decree, expressly reserving the rights of the Lackawanna Company, which rights are, as we have before stated, reserved by every decree and decretal order in this cause and in Causes Nos. 198 and 185, up to and including the final decree in Cause No. 227. Under the decree, under which he bought, and under the reservations in the same, Downs stands absolutely in the shoes of the Houston and Texas Central Railway Company, defendant, and we are entitled to have our rights adjudicated exactly as if Downs were not in the case.

III.

If the Court should conclude that neither the Farmers' Loan and Trust Company nor the Lackawanna Company has any lien on income, then the income in the hands of the Receiver must, necessarily, be pro-rated between the

different creditors of the defendant Company before the Court. In such an event, equality is equity.

We respectfully submit that all the assignments of error are well taken, and that the Lackawanna Company is entitled to a reversal of the judgment of the lower court, and to a decree in its favor ordering the payment, out of the funds in the custody of the Court, to said Lackawanna Company of the two sums of \$6,246.51 and \$99,300.64, with interest at six per cent. per annum from May, 1885, until paid; or, if the Court should conclude that neither the Lackawanna Company nor the Farmers' Loan and Trust Company has established any lien in the premises, then the cause should be remanded to the lower court with instructions to divide the income in the hands of said Court, after payment of all costs and expenses, between the different creditors of the defendant corporation before the Court pro rata.

Respectfully submitted,

E. B. KRUTTSCHNITT,

E. H. FARRAR,

B. F. JONAS,

H. T. GURLEY,

*Solicitors and of Counsel for Lackawanna
Coal and Iron Co.*

N. O., DEC. 30, 1896.

N^o. No. 22.

Brief of Kruttschnitt and Evarts

Petitioners

Supreme Court of the United States.

OCTOBER TERM, 1898.

Filed Feb. 23, 1899.

No. 122.

THE LACKAWANNA IRON AND COAL COMPANY ET AL.,
Intervenors and Petitioners,
against

THE FARMERS' LOAN AND TRUST COMPANY ET AL.,
Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT
OF APPEALS FOR THE FIFTH CIRCUIT.

Brief on Behalf of the Petitioners.

E. B. KRUTTSCHNITT,
MAXWELL EVARTS,
Of Counsel for Petitioners.

Supreme Court of the United States.

OCTOBER TERM, 1898.

No. 162.

THE LACKAWANNA IRON AND COAL CO.

ET AL.,

Intervenors and Petitioners,

AGAINST

THE FARMERS' LOAN AND TRUST CO.

ET AL.

Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES
CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT.

BRIEF ON BEHALF OF THE PETITIONERS.

Statement.

The Houston and Texas Central Railway Company, a corporation of the State of Texas, owned at the time of its failure about 520 miles of railway in that State, consisting of a Main Line from Houston to Denison, a branch line from Hempstead to Austin, called the Western Division, and a branch line from Bremond to Ross, called the Waco and Northwestern Division (Rec., p. 3). This Waco and Northwestern Division was 58 miles in length, and is the division in respect of the income of which the petitioners claim an equitable lien for the value of steel rails laid on the line shortly before the failure of the Company, claiming also that such equitable lien is superior to the claims of the bondholders in respect of such income.

The property of the Company was subject to the liens, of seven mortgages, known, respectively, as the Main Line First Mortgage, Western Division First Mortgage, *Waco and Northwestern Division First Mortgage*, Main Line and Western Division Consolidated Mortgage, Waco and Northwestern Division Consolidated Mortgage, Income and Indemnity Mortgage and General Mortgage (Rec., p. 3). The present intervention was filed in a suit brought by the Farmers' Loan and Trust Company, as Trustee, to foreclose the Waco and Northwestern Division First Mortgage.

On January 1, 1885, the Company made default in the payment of interest on its First Mortgage bonds (Rec., p. 105), and in February, 1885, Receivers of the properties of the Company were appointed by the United States Circuit Court for the Eastern District of Texas as hereinafter stated.

Between February and May, 1884, there were delivered by the petitioner new steel rails which were subsequently laid upon this Waco and Northwestern Division, which replaced 30.8 miles out of the 58 miles constituting that Division.

The building of the Houston and Texas Central Railway was begun in 1857, and completed in 1875 (Rec., p. 104), and prior to 1883 (with the exception of about 5,000 tons, *i. e.*, about 55 or 60 miles out of 520 miles, the length of the entire road), no new rails had been laid in any of its tracks since the road was first built. The condition of the road at the time when the new steel rails purchased under contracts with the petitioner as hereinafter stated were laid in the track is shown by the petition at page 78 of the record, as follows :

" That all of said steel rails so delivered were used for the useful improvement and necessary repair of the Main Line of said Houston and Texas Central Railway Co. and of the Western division thereof, and of the Waco and Northwestern divis-

ion thereof, to the extent hereinafter more fully set forth. That said steel rails were so absolutely necessary to said company to enable it to replace the old iron with which its tracks were laid that it is doubtful whether said company could have maintained its existence as a common carrier without them. That prior to the improvement and repair of said line of road with steel rails, as aforesaid, accidents to life and limb and damage to property was so great, owing to the condition of the tracks of said company, that the name of the Houston and Texas Central Railway Company became a terror to the traveling and shipping public, and a byword and a reproach. That by means of said steel rails so furnished by petitioner to said defendant railway, the railway of said defendant company has been kept in safe running order, its business and importance increased, and said railway thereby rendered more valuable to the bondholders under the various mortgages thereupon, and especially to the bondholders under the deed of trust and mortgage held by complainant herein, and upon which its bill of foreclosure has been filed in this cause. That said indebtedness was contracted by defendant in consideration of its promise to pay the same out of the earnings of its railway. That your petitioner made the contracts aforesaid and furnished the steel rail aforesaid under the expectation and belief that it would be paid for the same out of the revenues and earnings of said property; and that in case said revenues should not be sufficient, out of the proceeds of the sale thereof, by preference over any of the holders of mortgage bonds secured by deeds of trust on said property, but that said defendant, instead of paying the debt so justly due to your petitioner, out of the earnings of said railway, has entirely failed to pay the same or any part thereof,

as hereinabove set forth ; and that the truth is, and your petitioner so charges, that the said defendant has used a large amount of said earnings for the payment of coupons upon bonds secured by the mortgage, upon which a bill of foreclosure has herein been filed, although the holders of said coupons were only entitled to receive payment thereof after the defendant had paid your petitioner the amounts advanced and expended in the manner and for the purposes hereinabove set forth. That said steel rails so purchased by said railway company were actually used for the betterment and improvement of its railway aforesaid, and not for purposes of construction ; and that the said rails have been an increment to the value of the property mortgaged to said bondholders, and that your petitioner has the right to claim, and does claim, that the revenues of said railway property should be applied to the payment of petitioner's said indebtedness, by preference over the claim of any bondholders or coupon holders whomsoever."

The Special Master, appointed by the Court to report upon the intervention in this cause of the Lackawanna Company, found

" that, at the time when the contracts hereinbefore mentioned were entered into between said Lackawanna Company and the defendant Railway Company, *that the condition of the track of the defendant railway company was such that the demand for new rails upon the most worn portion of the roadway was practically imperative. * * * The condition of these roads was bad, except such portions as had been relaid with 5,000 tons of rails purchased prior to December 28, 1882. There was continual breakage of rails and wrecking of trains ; the track was unsafe, and was generally so regarded, not only by 'railroad men,' but by the*

traveling public; the damage to merchandise, rolling stock, etc., was continuous, and the need for new rails appears to have been 'absolutely necessary as a preservation of human life,' the loss of which was liable to occur at any moment" (Rec., p. 104).

The contracts between the Lackawanna Company, the intervenor and petitioner herein, and the Railway Company were made under date of December 28, 1882, April 26, 1883, and October 30, 1883, respectively, and provided for the furnishing by the intervenor of about 20,000 tons of steel rails to be laid in the track of the Railway Company.

CONTRACT OF DECEMBER 28TH, 1882.

All amounts due under this contract have been paid.

CONTRACT OF APRIL 26TH, 1883.

No claim is made to recover the small balance due for rails furnished to the Waco and Northwestern Division of the Railway Company under this contract as it is impossible to state positively how many of the rails delivered thereunder were actually used upon that Division.

CONTRACT OF OCTOBER 30TH, 1883.

Under this contract rails were delivered during the months of February, March, April and May, 1884, the purchase price of which was, under the terms of the contract, evidenced by Notes maturing six months from date of delivery, which Notes, by the terms of the contract itself, were subject to a right of renewal, which was exercised, so that the Notes became due in February, March, April and May, 1885 (Rec., p. 102). Of these rails an amount worth at the contract price \$99,300.64 was laid upon the Waco and

Northwestern Division. That is to say, 30⁸/₁₀ miles out of 58 miles (the length of the Waco and Northwestern Division) were laid with rails furnished under this third contract (Rec., p. 104). No security was stipulated or given by or under this contract, and the Special Master found :

“That when the aforesaid contracts were made with the said Lackawanna Company, both seller and buyer expected the debts to be paid from the net income of the Railway. That the credit extended under said contracts was at the request of and for the accommodation of the defendant railway company and upon its general credit. That said sales were made without any stipulation that security should be given by the defendant company for said rails or that payment therefor should be made out of any particular fund or in any particular way; that said sales were for an unusually large amount of rails, and the defendant was unable [to] pay cash therefor, and there was no other way of obtaining said rails except upon credit” (Rec., p. 104).

Prior to the date of maturity of any of the Notes issued under this third contract all the railways of the Houston and Texas Central Railway Company were placed in the hands of Receivers, and the Waco and Northwestern Division there remained at the time of the making of the decrees in the Circuit Court and Circuit Court of Appeals brought up by this *certiorari*. Pending determination of this *certiorari* proceeding there has been reserved in the registry of the Circuit Court an amount sufficient to pay the balance due for the steel rails involved in this proceeding.

The Receivership at first of all the properties of the Houston and Texas Central Railway Company, and thereafter of the Waco and Northwestern Division only, underwent certain changes and modifications from time to time in the various equity causes upon the

docket of the United States Circuit Court for the Eastern District of Texas, known as "Cause No. 185," "Consolidated Cause No. 198" and "Cause No. 227." The history of these three cases was as follows :

RECEIVERSHIP IN CAUSE NO. 185.

On February 16, 1885, the Southern Development Company, a corporation organized under the laws of the State of California, in its own behalf and in behalf of all other persons similarly situated, who might intervene in the suit to protect their own interests, filed its bill of complaint against the Houston and Texas Central Railway Company in the United States Circuit Court for the Eastern District of Texas, claiming a lien upon the net earnings of the railway company and all its properties superior in rank to the Mortgage Bonds. Under this bill Benjamin G. Clark and Charles Dillingham were appointed Receivers on the 21st day of February, 1885. Thereafter, and on or about the 18th day of April, 1885, the Southern Development Company filed an amended and supplemental bill, in which it made defendants Nelson S. Easton and James Rintoul and the Farmers' Loan and Trust Company, in their capacities as trustees of the various mortgages upon the property of the railway company.

The Lackawanna Company, on the 12th day of September, 1885, by permission of Court, filed a petition of intervention in this cause No. 185, praying that it might be allowed to intervene for its interests and join the complainant the Southern Development Company, and become itself a party complainant to said bill and amended and supplemental bill against all of the defendants therein, and it was further prayed in said intervening petition that the sum found due to said petitioner might be ordered to be paid out of the revenues of the defendant company, and might be declared a lien thereon and upon all the property of the railway

company superior in rank to the claims of the mortgage trustees and to the mortgage bonds and coupons issued under their various deeds of trust (Rec., pp. 105-108).

To the bill and amended and supplemental bill of the Southern Development Company there were filed by the defendant trustees general and special demurrers which were sustained by the Court, and the bill and amended and supplemental bill were dismissed on the 27th day of May, 1886, without prejudice to the rights of the complainants (the Southern Development Company and the Lackawanna Company) to assert their claims in such manner as they might be advised (Rec., p. 108).

The Farmers' Loan and Trust Company appeared in cause 185 only as defendant and filed its answer to both the original and supplemental bills of complaint therein. An inspection of this answer will show and the Master finds that its averments are all defensive, and it does not appear from said answer that the Farmers' Loan and Trust Company either demanded of the Court that the Receiver should hold the property for said trustee or that it in any other manner demanded any affirmative relief. Its appearance in said cause No. 185 was simply that of a defendant in opposition to the rights asserted in the original and supplemental bills of complaint (Record, pp. 115 and 116).

The Receivership under this bill continued until the 10th of July, 1886, and there was collected from the operation of the Houston and Texas Central Railway Company an amount of \$423,142.16 over and above operating expenses, taxes, etc. (Rec., p. 112).

The Receivers further collected from assets of the defendant railway company, consisting of traffic balances, sales of old rails and old cars, a sum total of \$265,921.42 (Record, p. 112).

The Receivers sold the rails removed from those portions of the Waco and Northwestern Division upon which the new steel rails furnished by the intervening petitioner were laid; 2,960 tons of such old rails were

removed from the 37 miles laid with new steel rails, and were sold at a price of \$13 per ton, net. *This would give a salvage of \$32,032 from the sale of old material removed from the 30.8 miles of road upon which new rails furnished by the Lackawanna Company under the contract of October 30th, 1883 (the Third Contract), were laid* (Record, p. 104).

RECEIVERSHIP IN CAUSE NO. 198.

Prior to the dismissal of the bill in cause No. 185 the defendants therein, Nelson S. Easton and James Rintoul, on the 21st of January, 1886, filed two bills in equity in the United States Circuit Court for the Eastern District of Texas in causes known as Nos. 198 and 199, for the foreclosure and sale of the railway property covered by the Main Line First Mortgage and the Western Division First Mortgage (Rec., pp. 108 and 109).

Thereafter, and on the 18th of April, 1886, the Farmers' Loan and Trust Company filed a bill in equity in the same Court in the cause known as No. 201, for the foreclosure of the general mortgage (Rec., pp. 108 and 109).

On the 26th day of May, 1886, the day before cause No. 185 was dismissed, an order was entered consolidating Nos. 198, 199 and 201 under the number 198, and upon the same day another order was entered appointing Nelson S. Easton, James Rintoul and Charles Dillingham receivers of all the property of the railway company and directing Clark and Dillingham as receivers in cause No. 185 to immediately transfer and deliver all the property held by them as such receivers to the receivers appointed in the consolidated cause No. 198 (Rec., p. 109).

On the 26th of November, 1886, the Lackawanna Company filed its petition of intervention in said Consolidated Cause No. 198 praying substantially for the same relief against all the railways, revenues, earnings and other properties of the railway company, including

the railways, revenues and earnings of the Waco and Northwestern Division thereof, as was prayed for by petition of intervention filed in said cause No. 185, and as is prayed for by its petition of intervention now before this court (Rec., p. 113).

A report was filed upon the petition of the Lackawanna Company in consolidated cause No. 198 by the special master appointed therein finding that under the facts of the case the debt for which said Company filed its petition "was of a character equitably entitling it to be discharged in preference to the debt embraced in the mortgages represented" in said consolidated cause (Rec., p. 113). To this report the Farmers' Loan & Trust Company, complainant in consolidated cause No. 198 filed exceptions, but said exceptions were never brought to a hearing and the same are still pending (Rec., p. 114).

A final decree of foreclosure was rendered in consolidated cause No. 198 on the 4th day of May, 1888, and the property was sold under this decree on the 8th of September, 1888, at Galveston, Texas, and the Waco and Northwestern Division was purchased by George E. Downs subject to the Waco and Northwestern First Mortgage, which is the mortgage involved in the present suit in which this petition of intervention was filed (Rec., p. 117).

In said final decree in consolidated cause No. 198 the court expressly reserved the right to charge the property ordered to be sold under said decree with any amounts that it might decree in favor of any intervention then on file, which of course included the intervention of the Lackawanna Company which was on file at the time of said decree (Rec., p. 117).

Afterwards and on the 20th day of April, 1889, the Lackawanna Company filed its petition in consolidated cause No. 198 asking that the receivership should continue and remain over the property then in the possession of the court until the claims and demands of the

Lackawanna Company upon said property should have been finally decreed upon, and if decreed in its favor should have been finally paid and settled. Upon this petition an order was entered directing the Receiver to retain possession of said property until the further order of the Court and further ordering that the receivership which had theretofore been ordered in cause No. 227 hereinafter referred to should be concurrent with the original receivership ordered in Consolidated Cause No. 198 and that the Receiver should keep separate accounts of the earnings and expenses of the Waco and Northwestern division of the railway company (Rec., p. 118).

In Consolidated Cause No. 198, the Farmers' Loan and Trust Company expressly assented to appear as complainant in cause 198, *but filed no bill of complaint therein as Trustee of the first Mortgage of the Waco and Northwestern Division*, and the bill of complaint filed by the Farmers' Loan and Trust Company in Cause No. 227 was not filed until long after the final decree in Consolidated Cause No. 198.

On March 21, 1887, the Farmers' Loan and Trust Company as Trustee under the Waco and Northwestern First Mortgage, filed an answer to the petition of Nelson S. Easton and James Rintoul in Consolidated Cause No. 198, praying the Court that any order which should be entered in Consolidated Cause No. 198 directing the payment by the Receivers out of the surplus of net earnings in their hands of any coupons falling due under any of the Trust Deeds executed by said Railway Company should provide for the payment by the Receivers out of the surplus of net earnings in their hands of the two coupons due under the Waco and Northwestern Division First Mortgage as well as under the other mortgages (Record, pp. 115-117).

Upon this application of the Farmers' Loan and Trust Company an order was entered on the 27th day of April, 1887, in said Consolidated Cause No. 198, directing that the coupons due January 1, 1885, and July 1, 1885, upon the First Mortgage Bonds of the Waco

and Northwestern Division should be paid with interest upon said coupons due January 1, 1885, from January 1, 1885, until May 1, 1887, at the rate of six per cent. per annum, and with interest upon one-half of the coupons due July 1, 1885, from said last-named date until May 1, 1887, when the same was ordered to be paid, and upon the remaining one-half of said coupon until it should have been paid. The two coupons, amounting altogether to \$91,371 (Rec., p. 121), were paid in pursuance of this order which expressly declared that it was

“ Without prejudice to the rights of defendant or of any intervenor in this cause or any final decree to be rendered in the same, nothing herein being decided as to the merits of the claim of the defendants or of intervenors and this order not in any manner stopping or affecting the rights of any party or intervenor in this cause ” (Rec., p. 117).

The Farmers' Loan and Trust Company, as Trustee of the First Mortgage of the Waco and Northwestern Division, also filed petitions in the United States Circuit Court for the Eastern District of Texas, on the 6th day of November, 1888, and on the 20th day of November, 1888, for payment of the remaining coupon interest due upon the Waco and Northwestern Division First Mortgage, but upon these petitions no order was ever entered (Rec., p. 117).

The Receivers in Consolidated Cause No. 198 during their administration realized out of proceeds of sale or collection of old assets of the defendant company the sum of \$135,889.70 (Record, p. 113).

The Receivers, in suits Nos. 185 and 198, during their administration, expended a sum total of \$1,536,116.38 outside of operating expenses, all of which, except the sum of \$23,274.20, clearly went into the pockets of the mortgage creditors, or was expended in betterments upon the properties mortgaged to them.

In other words, a total of \$1,512,842.18 of the revenues of the Receivership inured to the benefit of the mortgage creditors (Record, p. 112).

The accounts of the defendant Railway Company and of its Receivership, prior to April, 1889, were not kept in such a manner as to distinguish between earnings and expenses on the Waco and Northwestern Division, and those derived from the other divisions of defendant Company's railway (Record, p. 121).

RECEIVERSHIP IN CAUSE NO. 227.

On the 6th day of April, 1889, the Farmers' Loan and Trust Company, as complainant, filed its bill in equity against the Houston and Texas Central Railway Company and others seeking the foreclosure of the Waco and Northwestern Division First Mortgage (Rec., p. 2). *The filing of the bill on April 6th, 1889, was the first attempt by the Farmers' Loan and Trust Company, as trustee, to enforce its rights under this mortgage upon either corpus or income of the property mortgaged thereby.*

In this suit the Lackawanna Company on the 3d of November, 1891, filed the petition of intervention now before this Court (Rec., p. 75), the object of which was to obtain the recognition of an indebtedness due to it by the railway company, and represented by 25 promissory notes maturing during the first five months of 1885 and aggregating a total of \$445,175.50 face value. The amount of this indebtedness (including therein accrued interest) had previously been established by a judgment of the District Court at Dallas County, Texas, at the sum of \$555,914.25 with interest at eight per cent. per annum from May 17, 1889 (Rec., p. 86).

These Notes represented the purchase price of the steel rails bought by the Railway Company from the Lackawanna Company under the circumstances above set forth.

The petition (Record, pp. 86, *et seq.*), after reciting

the facts constituting the claim of the Lackawanna Company, asked that an account might be taken, under the direction of the Court, as to the amount due to the petitioner by the Railway Company and as to the dates and amounts of money paid by the defendant Railway Company to any of the mortgagees in the various trust deeds, described in the petition, showing*particularly the issue of bonds upon which such interest was paid ; and what proportion of the amounts so paid were paid out of current revenues of the Company, in the absence of earnings, and what amounts were so paid out of net earnings of the defendant Railway Company ; and particularly so as to show what amounts and proportions were so paid out of the net earnings of those portions of the railway of the defendant Railway Company, described in the Bill of Complaint of the Farmers' Loan and Trust Company, hereinabove referred to ; that an account might be taken showing the proportion of steel rails furnished by petitioner to the defendant Railway Company, used upon the railways described in the Bill of Complaint ; and that the account to be taken should also show all receipts and expenditures made by the Receivers, in whose hands the property had been placed under the various insolvency proceedings hereinbefore referred to, and which account should be taken in such manner as to show the dates when the expenditures were made, and the character of the expenditures, and in such manner as to show whether the expenditures were made for operating and running expenses, or for extraordinary repairs, betterments and improvements of the property or for the payment of fixed charges upon the same.

The petition further prayed that for the amounts due on such accounting to petitioner and equitably chargeable upon the railways described in the Bill of Complaint in said cause, there might be a decree against the defendant Railway Company, and against all of the parties complainant and defendant, decreeing

the sum so due to be liens upon the net earnings of the Railway Company, and especially upon those portions of said net earnings which have accrued or may accrue from the railways described in the Bill of Complaint, both those accrued prior to and during the Receivership in Cause No. 185, and those accrued and to accrue during the Receivership in Consolidated Cause No. 198, and upon all of the property of the Railway Company, superior in rank to the claims of the trustee and of the holders of mortgage bonds and coupons issued under the deed of trust sought to be foreclosed by the Farmers' Loan and Trust Company; that the net earnings of the railway described in the Bill of Complaint should be first devoted to the payment of the amounts so decreed, and, if they should prove insufficient to pay the amounts, then that the Court should decree the payment of said amounts out of any proceeds of sale of the property of the defendant Railway Company to be made under final decree (Record, pp. 86-88).

The Pacific Improvement Company, as assignee of the Lackawanna Company upon its petition, and by order of Court, dated February 5th, 1892, was made a co-petitioner with the Lackawanna Company (Record, pp. 96, 97).

This petition of intervention, with the answers of the Farmers' Loan and Trust Company, and of Moran Bros. *et als.*, intervening bondholders (Record, pp. 88 and 97, 98), was referred to William L. Prather as a special master "to take the accounts in said petition prayed for, and to investigate, and to find and report upon the facts as to the subject matter of said petition, and of the answers thereto" (Record, p. 98).

On the 13th of January, 1896, the Special Master filed his report upon the intervention of the Lackawanna Company finding the facts substantially as they have been hereinbefore stated (Rec., p. 98, *et seq.*) and especially finding as to the equitable nature of the

claim of the Lackawanna Company at page 104 of the Record as follows :

“ It appears that at the time when the contracts hereinbefore mentioned were entered into between said Lackawanna Company and the defendant railway company that the condition of the track of the defendant railway company was such that the demand for new rails upon the most worn portion of the roadway was practically imperative. For a number of years prior to December, 1882, only about 5,000 tons of new rails had been purchased. The road north from Houston for 90 miles was built in 1857-1861 and thence northward to Denison, 1867-1872. The Western division leading to Austin was constructed in part prior to 1861, and completed in 1873, and the Waco division was completed about 1875. The condition of these roads was bad, except such portions as had been relaid with 5,000 tons of rails purchased prior to December 28th, 1882. There was continual breakage of rails and wrecking of trains, the track was unsafe and was generally so regarded, not only by ‘ railroad men,’ but by the traveling public; the damage to merchandise, rolling stock, &c., was continuous, and the need for new rails appears to have been ‘ absolutely necessary as a preservation of human life, the loss of which was liable to occur at any moment.’

“ I find that when the aforesaid contracts were made with the said Lackawanna Company both seller and buyer expected the debts to be paid from the net income of the railway; that the credit extended under said contracts was at the request of and for the accommodation of the defendant railway company and upon its general credit. That said sales were made without any stipulation that security should be given by the

defendant company for said rails, or that payment therefor should be made out of any particular fund or in any particular way; that said sales were for an unusually large amount of rails, and the defendant was unable to pay cash therefor, and there was no other way of obtaining said rails except upon credit."

At the time of the Special Master's report, filed January 6, 1896, the Circuit Court had in the hands of its Receiver, or deposited in the registry of the court net income to the amount of \$362,855.37, which had accrued from the Waco and Northwestern Division alone between December 10, 1892, and September 3, 1895 (Rec., last few lines of p. 58, and last half of p. 65).

Upon this report a decree was entered on the 26th of February, 1896, dismissing the petition of intervention of the Lackawanna Company and its transferee, the Pacific Improvement Company, without prejudice to their rights under the intervention in the Consolidated Cause No. 198 (Rec., pp. 121 and 122).

From this decree an appeal was taken to the United States Circuit Court of Appeals for the Fifth Circuit, which court affirmed the decree of the lower court (Rec., p. 140). The intervention of the Lackawanna Company now comes before this court upon a writ of *certiorari*.

MATERIAL FACTS AND DATES.

October 30th, 1883. Date of contract under which rails were delivered.

February to May, 1884. Date of delivery of rails.

February 21st, 1885. Receivers appointed in Cause No. 185.

September 12th, 1885. Petition of intervention filed by Lackawanna Company in Cause No. 185. Ever since this date an intervention on behalf of the Lackawanna Company has been pending for the same claim in the various receivership proceedings.

May 26th, 1886. Order entered consolidating causes 198, 199 and 201 in one cause known as Consolidated Cause No. 198.

November 26th, 1886. Petition of intervention filed by Lackawanna Company in Consolidated Cause No. 198. Exceptions to report on this petition are still pending.

May 4th, 1888. Final decree of foreclosure in Consolidated Cause No. 198.

April 6th, 1889. Bill filed in present cause to foreclose Waco and Northwestern Division First Mortgage.

November 3d, 1891. Petition of intervention filed by Lackawanna Company in present cause. The same claim is made upon this intervention as was contained in the petition filed in Cause No. 185 on the 12th of September, 1885, and in the petition filed in Consolidated Cause No. 198 in November, 1886.

During the years 1883 and 1884 when the rails were contracted for and delivered \$2,386,400 interest was paid out on bonded indebtedness of the railway company. Of this sum upwards of \$1,300,000 was paid from income or current earnings, and out of the total amount, \$159,600 was paid as interest on the Waco and Northwestern Division First Mortgage Bonds (Rec., p. 119).

The receivers in Causes Nos. 185 and 198 received about \$32,000 for proceeds of iron rails replaced with the steel rails involved in this claim (Record, p. 104) and expended \$1,512,842.18 for purposes outside of their operating expenses to pay off the mortgage interest or to pay for rolling stock or betterments upon the mortgaged properties; and during the receivership in Cause No. 198 \$91,371 was paid under order of the court to holders of Waco and Northwestern Division First Mortgage Bonds, the order for such payment expressly stating that such payment was without prejudice to the rights of this intervenor (Rec., pp. 112 and 114).

The Waco and Northwestern Division constituted $11\frac{13}{100}$ per cent. of the Houston and Texas Central Railway system (Rec., p. 3).

At the time of the Special Master's report, filed January 6, 1896, the Circuit Court had in the hands of its Receiver, or deposited in the registry of the court, net income to the amount of \$362,855.37, which had accrued from the Waco and Northwestern Division alone between December 10, 1892, and September 3, 1895 (Rec., last few lines of p. 58 and last half of p. 65).

SPECIFICATION OF ERRORS.

FIRST. The court below erred in not adjudging and decreeing that the petitioners had a lien upon the income now in court of the Waco and Northwestern Division of the Houston and Texas Central Railway Company, for rails furnished by the Lackawanna Company to and laid upon said division, superior to any lien thereon of the Waco and Northwestern Division First Mortgage.

SECOND. The court below erred in not adjudging and decreeing that said petitioners had a lien upon the corpus of the property of said Division of said Railway Company superior to the lien of said mortgage.

THIRD. The court below erred in adjudging and decreeing that the petitioners had no lien for the rails so furnished as aforesaid upon the said income or property of said Division of said Railway Company.

FOURTH. The court below erred in not adjudging and decreeing that, if the petitioners had no lien upon the said income, the same should be distributed ratably between the petitioners and the creditors of the railway company secured by the said Waco and Northwestern Division First Mortgage.

FIFTH. The court below erred in adjudging and decreeing that the said Waco and Northwestern Division First Mortgage was a lien upon the income in court earned by said Division of said Railway Company.

FIRST POINT.

A materialman who furnishes to a railroad supplies which save and preserve the property and enable it to continue as a "going concern" has an equitable lien upon the income and the corpus of the property superior to that of the mortgage creditors.

In the consideration of this question it is useful to have continuously and distinctly in mind the character of a great railroad property and no better idea of it can be conveyed than that given by Mr. Justice BLATCHFORD in *Union Trust Co. vs. Illinois Midland Co.*, 117 U. S., 434, 455, when he said :

"A railroad and its appurtenances is a peculiar species of property. Not only will its structure deteriorate and decay and perish, if not cared for and kept up, but its business and goodwill will pass away if it is not run and kept in good order."

The situation of the Houston and Texas Central Railway Company at the time the rails in question were sold to it by the Lackawanna Iron and Coal Company is of importance. The facts in the case at bar make it somewhat different from the usual run of cases decided by this Court, which involve the doctrine of *Fosdick vs. Schall*, 99 U. S., 235, and the furnishing of the rails to the railway company was not the ordinary case of a periodical renewal of supplies to make good the usual wear and tear upon a railroad, or the sale of coal to furnish fuel for its engines. In this case, in addition to the fact that the rails furnished kept the railway company a "going concern," we find that the sale of the rails actually saved and preserved the property and enabled the railway company to continue its existence. The new rails not only permanently improved

the mortgaged property, but the railroad and its receivers realized a considerable sum of money from the sale of the old rails, which were replaced by those sold by the petitioner. As the record shows, the track of the railway company was worn out. Prior to the purchase of the rails from the Lackawanna Company it had become dangerous to travel upon the road and the general public hesitated to use it, even for the shipment of freight. It was doubtful if the railway could have continued longer in existence, and to preserve its property and continue in business it purchased the rails in question. There was substantially a retracking of the entire system. The Waco and Northwestern Division of the Houston and Texas Central Railway Company was fifty-eight miles in length. Nearly thirty-one miles of this division were relaid with rails furnished under the contract involved in this case, dated October 30th, 1883 (Rec., p. 104).

The Lackawanna Company, with a full knowledge of the situation, and appreciating the importance to the railway company of the supplies furnished, sold the rails, took no collateral security for the notes given for the amount due it, expected to be paid out of the income of the railway company as had been done under the first of the two prior contracts, and as was being done under the second, and relied upon the fact that its supplies saved and preserved the property for the benefit of the railway company, kept it a going concern and conferred an equal benefit upon its mortgage creditors, and that, by reason of such circumstances, there arose an equitable lien in its favor upon the property and more especially upon the income of the railway company, which gave it a preference over the mortgage.

The broad principle of equity which we think should control this case is that any man who furnishes to another at his request money, labor or supplies for the purpose of saving and preserving the

property of the latter is entitled to be repaid for his advances (whether such advances are in the shape of money, labor or supplies) before the other can take the benefit of his gain. As we understand it, such equitable principle and the equitable lien so created is as good against the mortgagee of the property preserved and saved as against the mortgagor, for (1) the mortgagee is equally benefited with the mortgagor by the supplies furnished, and (2) the mortgagee, by leaving the mortgagor in charge of the mortgaged property makes him his agent to create any lien necessary and proper to save and preserve the property and keep it a "going concern."

Fosdick vs. Schall (*supra*) was the first railroad foreclosure case which contained a statement of this equitable doctrine, but it has been often applied in foreclosure suits involving other property.

I.

PROPERTY SAVED AND PRESERVED BY MATERIALS AND SUPPLIES FURNISHED AT THE REQUEST OF THE OWNER IS SUBJECTED TO, AND CHARGED WITH, A LIEN AS AGAINST THE OWNER FOR THE VALUE THEREOF.

Before, therefore, taking up the discussion of Fosdick vs. Schall and the subsequent kindred cases decided by this Court involving railroad foreclosures, it may be useful to refer to various cases which sustain the principle that any service rendered at the request of the owner which saves and preserves a property is in the nature of a salvage service and creates an equitable lien upon the property in favor of the party performing the service because of the fact that the owner of the property would have had nothing but for the service rendered and must, therefore, before taking advantage of such service, repay it.

In *Shearman vs. Assurance Co., L. R., 14 Eq., 4*, it appeared that one Thomas Pocknall had insured his life in the defendant company, and deposited the policy with the plaintiff *as a security for a debt* due from him to the plaintiff. Subsequently, Pocknall was adjudicated a bankrupt, which relieved him from any obligation to pay the premiums on the policy. He, however, continued to pay the premiums after his bankruptcy and up to the time of his death. A bill was filed by the plaintiff to recover the amount of the insurance money. The widow and legal representative of Pocknall also claimed the money, which was paid into court. It was eventually held that the plaintiff was entitled to the money, but must repay to the estate of Pocknall the premiums paid by him subsequently to the bankruptcy, on the ground that they were so much *salvage money*, and that the plaintiff would have had nothing at all but for the money advanced by Pocknall out of his own pocket. The Master of the Rolls said at p. 5 :

“That the plaintiff was clearly entitled to the policy moneys, but that the premiums paid subsequently to the bankruptcy were in the nature of *salvage moneys*, and that the plaintiff must repay them to Mrs. Pocknall, with interest at four per cent.”

It is true that in the case cited the property mortgaged was an insurance policy and not a railroad and that the supply man furnished money and not rails to save and preserve the mortgaged property, but aside from such apparently immaterial distinctions it is not clear why the case is not on all fours with the case at bar.

In the *Matter of Tharp, 2 Sma. & Giff., 578*, the Lord Chancellor, in deciding that the consignee of West India estates had a right to be reimbursed his

expenditure out of the rents of the English estates of the same owners, said at page 578 :

“ In Ireland, it is a very common equity to have, as a prior charge to all other incumbrances, what is called salvage money : Where a leasehold estate, or an estate held for lives to which half a dozen people are entitled in succession, many of them being mortgagees, according to certain priorities, the last man of all who is entitled after everybody, being in possession, redeems, I may say, the estate by paying the landlord, who otherwise would have recovered the estate and taken it from everybody : *this payment is what is called salvage money. That is an established equity, and a very proper equity. He that pays the salvage has a prior encumbrance to every other charge and interest, because, so far as any interest is left to anybody beyond the charge, it is acquired by that payment, in the shape of redemption money.*”

In *Minnitt vs. Lord Talbot*, L. R., Ir. 1 Ch. D., 143, money was advanced by members of a club to pay for improvements to the buildings of the club house and a bill was filed to recover it. The prayer of the bill was that the plaintiffs might be declared entitled to an equitable lien for the sums found due them upon the premises and furniture therein and all other property of the club. This lien was allowed by the Master of the Rolls, who said at page 152 :

“ In the name of common sense, could the Club have said ‘ we will not allow you to be repaid it, for we did not authorize you to advance it ; though it is true we authorized the improvements to be made, we only authorized them to be so made by borrowed money ; we have availed ourselves of them, we have played in the new billiard rooms and slept in the new bedrooms built with your

money, but we will not recoup you?' I think that the club could not be listened to for a moment in putting forward such an unconscionable proposition."

In the important and complicated litigation of *Manix, Assignee, vs. Purcell*, 46 Ohio St., 102, one of the questions was as to the right of a creditor to be reimbursed for certain repairs and improvements made by him upon a Roman Catholic cathedral at the request of the archbishop. There was apparently no agreement whatever as to any equitable lien, and an examination of the case, having regard to all the circumstances of the varied transactions in which over three millions of dollars belonging to the congregations of various churches were lost, precludes the idea that there was any understanding between the archbishop and the creditor, as to any lien in favor of the latter, as against the cathedral. It was held, that the claim should be paid out of the property, *upon the ground that the cathedral had been preserved by the services rendered*. The Court said, at page 147 :

"The claim of John G. Hendricks, another cross-petitioner below, and cross-petitioner in error in this court, stands upon ground distinct from all others. He obtained a judgment against John B. Purcell, also after the assignment, upon a claim composed in part of an indebtedness for money deposited to bear interest, and in part for improvements and repairs placed upon the cathedral, *and for its preservation*, at the request of the archbishop. We are all in accord upon the proposition that the latter claim possesses peculiar merit, upon the principal that the trust property should answer for the reasonable expense incurred in *its preservation* and necessary repair and improvement. We are not in accord, however, as to the means of effectuating this right. A majority of

the Court is of opinion that the remedy may be granted in this case, and for this purpose the judgment as to this claim is reversed, and the cause remanded for further proceedings upon this branch of the controversy."

Mr. Justice STORY in his work on equitable jurisprudence gives the doctrine for which we contend as follows :

" But courts of equity have not confined the doctrine of compensation or lien for repairs and improvements to cases of agreement or of joint purchases. They have extended it to other cases where the party making the repairs and improvements has acted *bona fide* and innocently, and there has been a substantial benefit conferred on the owner, so that *ex æquo et bono* he ought to pay for such benefit."

2 Story on Eq. Juris., p. 582, § 1237 (13th Ed).

The principle stated by Mr. Justice STORY seems to have met with the approval of the Court of Appeals of the State of New York in the case of *Perry vs. Board of Missions, etc.*, of Albany, 102 N. Y., 99. The plaintiff Perry advanced money to pay for certain improvements and repairs upon a house owned by the defendant. He had no specific lien whatever of any kind upon the premises, but the Court of Appeals held that the particular facts in the case entitled him to an equitable lien upon the premises, saying at pages 104 and 105 :

" It is objected by the appellant that the plaintiff is not, by reason of any of these facts, entitled to an equitable lien upon the premises for the benefit of which they were made. We are of a different opinion.

" The principle upon which a Court holds that

a vendor, who has not been paid, is entitled to a lien on the land sold is that it would be contrary to natural justice to allow a purchaser to retain an estate which he has not paid for, and it seems very clear that there is a like natural equity in favor of the plaintiff. It is true he did not sell the estate, but he added to it, *and by his expenditures upon it fitted it for the purpose for which it was intended.* A lien for the price of an estate sold exists without *any special agreement*, and by virtue of a doctrine merely of a court of equity. Here there is a special agreement, and also a case to which the doctrine applies. * * *

"SECOND. The plaintiff's case is within the general doctrine of equity, which gives a right equivalent to a lien, when, in no other way, the rights of parties can be secured. *The advances were directly for the benefit of the real estate; they were approved by the convention by whose directions the title was conveyed to the defendant, but neither the convention nor the defendant have incurred any corporate liability, and, while it may be said that the advances were made on the promise of, or in the just and natural expectation, that a mortgage would be given, it is also true that they were made on the credit of the property, for the improvement of which they were expended. The repairs and improvements were permanently beneficial to it, made in good faith, with the knowledge and approbation of the parties interested, and accepted by them, not as a gratuity, but as services for which compensation should be given. The plaintiff's right to remuneration is clear, and unless the remedy sought for in this action is given, there will be a total failure of justice.*"

In *Smith vs. Smith*, 51 Hun, 164 (affirmed in 125 N. Y., 224), the plaintiff erected a building upon land of the defendant, increasing the value of the

property to a considerable extent. There was an oral understanding between them that, if the plaintiff became in any way embarrassed, he might sell the building. Upon the defendant refusing to permit the sale of the property, the plaintiff brought an action to establish an equitable lien thereon for the money expended by him upon the building. This equitable lien was sustained by the Court, and its judgment affirmed on appeal, the General Term saying, at page 169 :

"This right or lien is founded * * * upon the fact that it would be contrary to natural justice to allow the defendant to retain the building erected upon her land by the plaintiff without compensating him for the money thus expended. The plaintiff expended his money for the direct benefit of the defendant's real estate. The building erected by him was a permanent improvement to such real estate. * * * The plaintiff's right to receive the amount thus expended by him seems to be clear, and unless the remedy awarded in this action be upheld, there will be a failure of justice. We think the plaintiff's case is within the doctrine held in the cases cited, which gives a right equivalent to a lien where the rights of the parties can be secured in no other way."

In *Bright vs. Boyd*, 1 Story Rep., 478, one of the questions was whether a *bona fide* purchaser of real estate, whose title afterwards turns out to be defective, is entitled to compensation for improvements made upon the land. It was held by Judge STORY that he was. In the course of his opinion he says at page 495 :

"Take the case of a vacant lot in a city where a *bona fide* purchaser builds a house thereon, enhancing the value of the estate to ten times the original value of the land under a title apparently

perfect and complete; is it reasonable or just that, in such a case, the true owner should recover and possess the whole without any compensation whatever to the *bona fide* purchaser? To me it seems manifestly unjust and inequitable thus to appropriate to one man the property and money of another who is in no default. The argument, I am aware, is that the moment the house is built it belongs to the owner of the land by mere operation of law; and that he may certainly possess and enjoy his own. But this is merely stating the technical rule of law, by which the true owner seeks to hold what, in a just sense, he never had the slightest title to; that is, the house. It is not answering the objection, but merely and drily stating that the law so holds. But then admitting this to be so, does it not furnish a strong ground why equity should interpose and grant relief? * * *

"To the extent of the charge, from which he has been thus relieved by the purchaser, it seems to me that the plaintiff, claiming under the purchaser, is entitled to reimbursement in order to avoid a circuitry of action to get back the money from the administrator. * * * I confess myself to be unwilling to resort to such a circuitry in order to do justice, where upon the principles of equity the merits of the case can be reached by affecting the lands directly with a charge to which they are *ex æquo et bono* in the hands of the present defendant clearly liable" (p. 498).

Admiralty decisions are of course in no way controlling in a court of equity, but the reason of the priority of maritime liens for repairs and supplies furnished a vessel in a foreign port, over a prior mortgage, is not far from the reason of the equitable rule in *Burnham vs. Bowen*, 111 U. S., 776—viz., that by such supplies and repairs the ship is kept a "going concern;" but, in any event, the following quotations from the

admiralty courts are interesting as stating the principle, which we seek to establish, upon equitable grounds in no way connected with admiralty and maritime liens.

In *Poland vs. The Spartan*, 1 Ware, 134, 138, Judge WARE said :

“ It is a general principle of law, extending to a great variety of cases, that a person who has, by his own labor, thus added a new value to a specific article, has a lien on the article for the value of his service. It is a right consonant to all ideas of natural equity, and is highly favored by the law. * * * Another general principle is that, when this sort of confusion of goods is produced at the request of the general owner, he that has given the last increment of value to the article is entitled to be first satisfied out of the common stock.”

In *Stevens vs. The Sandwich*, 1 Pet. Adm., 233, 238, the point is well put in these words :

“ The reason of the lien to ship carpenters for repairs, independent of considerations of policy, even among contending mortgagees, is that such services *preserve the specific thing from destruction*, and securing such subsequent creditors does not injure prior mortgagees or creditors, since the pledge is increased in value, in proportion to such services.”

In *The Felice B.*, 40 Fed. Rep., 653, certain repairs and supplies were furnished the vessel *after the breaking up of the voyage*. Thereafter the vessel was libeled by the holder of a bottomry bond, and sold by the Marshal. Upon the distribution of the proceeds, a question arose as to the priority of the claim of the materialmen and the lien of the bottomry bond. It was held by Judge BENEDICT that, on equitable principles, the materialmen had a prior claim, for the reason that

they had by their repairs increased the value of the ship. He said (at p. 654) :

“ As to the demand of the materialmen, objection is made in behalf of the bottomry holder that he is entitled to priority in payment over any debts due the materialmen for repairs and supplies, and for services rendered to the vessel subsequent to the breaking up of the voyage. In regard to these demands, which consist of actual repairs put upon the vessel, and which tended to increase her value, equity requires that such demands should be paid prior to the bottomry, for the reason that these repairs have gone to enhance by so much the proceeds of the sale of the vessel now in court, and cannot with justice be applied to the payment of the bottomry.”

Although the property involved in the cases just cited was a ship, yet the decision was placed upon grounds of equity, and not admiralty law, and the words of Lord CRANWORTH, in *Bristowe vs. Whitmore*, 9 H. L. C., 391, 404, are most applicable :

“ The ground on which I rest this opinion has no reference to any law peculiarly applicable to shipping. * * * The principle which must, I think, govern this case is one of universal application ; namely, *that where a contract has been entered into by one man as agent for another, the person on whose behalf it has been made cannot take the benefit of it without bearing its burdens.*”

In the opinion of the Circuit Court of Appeals in the present case, at page 140 of the Record, it is sought to weaken the position taken by the Lackawanna Coal Company by referring to the case of *Railway Company vs. Cowdry*, 11 Wall., 459, 482, in which Mr. Justice BRADLEY said : “ As to the other point giving priority to the last creditor for aiding to conserve the thing, all that

is necessary to say is that the rule referred to has never been introduced into our laws except in maritime cases, which stand on a particular reason."

An examination of the Cowdry case and of the other cases referred to by the Circuit Court of Appeals shows that the claims in each were for materials used in the *original construction* of a railroad and not in its repair, which is a very different proposition from the one now before the Court. It was said in the Cowdry case, at page 480 :

" On the part of Robert Pulsford it is objected that the decree does not give him a priority on that portion of the road which was laid with his iron. He contends that he is entitled to this * * * because his capital applied to the road conserved it and rendered it capable of being operated, which it would not have been otherwise ; hence, on the principle adopted by the civil and maritime laws of awarding priority to the last creditor who furnished necessary repairs and supplies to a vessel, he is entitled to priority. The counsel for Pulsford has furnished us with a very ingenious and learned argument on these points, but we cannot yield to their force."

It is sufficient to say that the argument advanced in favor of Pulsford in the Cowdrey case would have been without force even in an admiralty court, and if the subject matter of the foreclosure suit had been a ship and not a railroad. It has never been held in admiralty that a materialman who furnished the material for the construction of a ship had under the maritime law a lien which displaced a prior mortgage. The only lien known in admiralty for supplies and repairs, which is given precedence over a prior mortgage, is that which results from the furnishing such repairs and supplies in a foreign port as will enable the ship to continue her voyage, keep her a going concern and place her in a position to earn money to pay the interest on the mortgage.

In other words, the argument that materials used in the *original construction* of a property should be paid for ahead of a prior mortgage thereon, is no more recognized in a court of admiralty than it is in any other court, and for the very obvious reason that what goes into the original construction of a ship or a railroad, cannot possibly be said to preserve and keep in existence such ship or railroad, which is the basis both of the admiralty and equitable lien.

It will be observed how careful this court is in all the cases referred to by the Circuit Court of Appeals in its opinion in this case to indicate the distinction between material furnished for the *original construction* of a railroad and material furnished to preserve and keep in order a railroad already constructed and to keep it a "going concern," and this court has never yet held that the principle of admiralty law referred to did not apply to the case of supplies furnished a railway company in order that it might continue in existence.

In the case of Toledo, &c., Railroad Co. vs. Hamilton, 134 U. S., 296, an equitable lien superior to the mortgage was claimed for work done in the *original construction* of property belonging to the railroad company. This lien was not sustained, but the court distinguished the case from an equitable lien for material and work which saves and preserves a railroad as a going concern. This material difference was brought out at page 301, as follows :

"Neither did the fact of the construction of the dock, and the consequent improvement of the mortgaged property, give, as reported by the master, to Hamilton an equitable lien prior in right to the lien of the mortgage, or furnish equitable reasons why the legal priority belonging to the mortgage should be displaced. It is true cases have arisen in which, upon equitable reasons, the priority of a mortgage debt has been displaced in favor of even unsecured subsequent

creditors. See *St. Louis, Alton, &c., Railroad vs. Cleveland, Columbus, &c., Railway*, 125 U. S., 658, 673, in which many of these cases are collected and the equitable principles underlying them stated. But those principles have no application here. *The work which Hamilton did was in original construction, and not in keeping up, as a going concern, a railroad already built. The amount due him was no part of the current expenses of operating the road. There was, as to him, no diversion of current earnings to the payment of current expenses.*

"The distinction is so well expressed by Mr. Justice BLATCHFORD, in giving the opinion of the court in the case of *Porter vs. Pittsburg Steel Co.*, 120 U. S., 649, 671, that it is sufficient to quote his language : 'The claims of the appellees are for the *original construction* of the railroad. This is not a case where the proceeds of the sale of the property of a railroad, as a completed structure, open for travel and transportation, are to be applied to restore earnings, which, instead of having been applied to pay operating expenses and necessary repairs, have been diverted to pay interest on mortgage bonds and the improvement of the mortgaged property, the debts due for the operating expenses and repairs having remained unpaid when a receiver was appointed. The equitable principles upon which the decisions rest, applying to the payment, out of the proceeds of the sale of railroad property, of such debts for operating expenses and necessary repairs, are not applicable to claims such as the present, accrued for the *original construction* of a railroad while there was a subsisting mortgage upon it.' "

The application of the admiralty rule in equity cases was recognized by Judge BRADLEY in the case of the *Provident Institution vs. Jersey City*, 113 U. S., 506.

It is very evident that the citation from Judge BRADLEY's opinion in the Cowdrey case (*supra*), which was relied upon by the court below, was intended by Judge BRADLEY to apply only to the facts of that particular case, where an equitable lien on the principle of the admiralty law was claimed for work and materials used in the *original* construction of a railroad. The views of Judge BRADLEY upon the question, when arising in a case like the present, is shown when he said in *Provident Institution vs. Jersey City*, 113 U. S., 506, 516, that

“ The law which gives to the last maritime liens priority over earlier liens in point of time is based on principles of acknowledged justice. *That which is given for the preservation or betterment of the common pledge is in natural equity fairly entitled to the first rank in the tableau of claims.*”

In the case of *Williams vs. Gibbes*, 20 How., 535, the doctrine which we now urge was the real ground of the decision, viz., that a lien was created for money advanced for the preservation of property. The facts were these: One Williams had a share in the Baltimore Company, which company had a claim against the Government of Mexico. He became insolvent and his assignee sold and assigned the share to a man by the name of Oliver. Oliver, and his executors after his death, prosecuted the claim of the Baltimore Company against the Mexican Government, and recovered a large sum of money. It was subsequently held that the assignment of Williams' share in the Baltimore Company to Oliver was invalid, and that the interest therein remained in Williams and passed to his legal representative, the complainant, who brought suit to recover the proceeds of Williams' share. The question was as to the right of Oliver's executors to deduct the costs and expenses incurred in getting this sum of money and the value of Oliver's service in that

regard. The lower Court held that such expenses, etc., were in equity entitled to be deducted before paying over the money and the decree of the Court was affirmed on appeal. The Court said :

“ The proofs show that Oliver appointed agents to represent him at the Government of Mexico as early as March, 1825, and that these agencies were continued from thence down till his death in 1834 ; and that during all this time he kept up an active correspondence with them and others, and with our ministers at Mexico, and with his own government, on the subject. The justice of these claims had been acknowledged by the Government of Mexico as early as 1823-4, but no provision was made for their payment. They were regarded as of very little value, from the hopelessness of their recovery ; and it is perhaps not too much to say, upon the evidence, that in the absence of the vigorous and efficient prosecution of them by Oliver, they would have been worthless * * * The estate of Williams has never expended a dollar towards recovering it ; nor has Oliver ever received any compensation for his services. The amount may seem large, but we cannot say the Court below was not warranted in allowing it upon the proofs in the case of the great service rendered, and of the customary charges in similar cases ” (p. 540).

“ All the services and expenses, therefore, of Oliver, in his lifetime, in the prosecution of the claims of the Baltimore Company against the Government of Mexico, and of the litigation since encountered by his executors in respect to the share, have resulted in securing the proceeds of the same to the estate of Williams, the original shareholder. Williams in his lifetime, and his legal representative since, down till the fund was in court awaiting distribution, had taken no steps

for its recovery, nor had they been subjected to any expense. The whole of the services had been rendered, and expenses borne, by Oliver and his executors; and the question is whether, upon any established principles of law or equity, the Court below were right in taking into the account in the settlement between the parties these services and expenses. We are of opinion they were (p. 537). * * *

“ But it is said that these suits were defended by the executors, while claiming the fund in right of their testator, and hence for the supposed benefit of his estate; that the defense was not made in their character of trustees, and cannot, therefore, be regarded as a ground for charging the estate of Williams with the costs of the litigation.

“ The answer to this view is that, although in point of fact the defense was made under the supposition that the fund belonged to the estate of Oliver, yet, in judgment of law, it was made by them as trustees, and not owners, as subsequently judicially ascertained; and, as the costs and expenses were properly incurred in the protection and preservation of the fund, it is but just and equitable they should be made a charge upon it.

“ The misapprehension as to the right cannot change the beneficial character of the expense, when indispensable to its security. * * *

“ Another principle which we think applicable to this case is to be found in a class of cases where a *bona fide* purchaser, for a valuable consideration, without notice, has enhanced the value of the property by permanent expenditures, and has been subsequently evicted by the true owner, on account of some latent infirmity in the title. It is well settled, if the true owner is obliged to come into a court of equity to obtain relief against the purchaser, the Court will first require reasonable compensation for such expenditures to be made,

upon the principle that he who seeks equity must first do equity (2 Story Eq., Secs. 799 and 7996; 6 Paige R., 403, 404; 1 Story Rep., 494, 495).

"A kindred principle is also found in a class of cases where there has been a *bona fide* adverse possession of the property tacitly acquiesced in by the true owner. The practice of a court of equity in such cases does not permit an account of rents and profits to be carried back beyond the filing of the bill (8 Wheat., 78; 27 E. L. and E. Rep., p. 212; 7 Ves., 541; 1 Ed. Ch., 579). This principle is applicable where the person in possession is a *bona fide* purchaser, and there has been some degree of remissness, or negligence, or inattention on the part of the true owner, in the assertion of his rights" (pp. 538 and 539).

The cases to which we have referred the Court would seem to conclusively show that the Lackawanna Company had an equitable lien as against the railway company for the value of the rails sold. This lien is against and upon the income and corpus of the property of the railway company which has been saved, preserved, improved and made valuable by the rails sold to the railway company by the Lackawanna Company, and is based upon the theory, (1) that any improvement put upon property by one not the owner, at the owner's request, creates a lien in his favor as against the owner for the reason that, as between the two, equity can see no justice in "appropriating to one man the property and money of another," and (2) upon the doctrine that services rendered, by which property is saved and preserved from total or partial destruction, must be repaid before the party benefited can take advantage of his gain.

II.

THE MORTGAGE CREDITORS, BY LEAVING THE RAILWAY COMPANY IN POSSESSION OF THE PROPERTY, IMPLIEDLY AUTHORIZED IT TO CREATE ANY LIENS THEREON WHICH MIGHT BE NECESSARY TO KEEP UP THE PROPERTY, AND ENABLE IT TO CONTINUE TO EARN THE INTEREST UPON THE MORTGAGED DEBT.

If we are correct in our conclusion that the circumstances of this case created an equitable lien in favor of the Lackawanna Company against the railway company for the value of these rails, the next question which presents itself is whether such lien is entitled to a preference over a prior mortgage.

The reasons why liens (and it is immaterial whether such liens are equitable or common law or of any other nature) created by a mortgagor in possession of property should be preferred to the mortgage are sufficiently obvious and require no extended discussion.

Stated briefly they are as follows :

FIRST. When the mortgagee leaves a mortgagor in possession of property such as a railroad, a ship or any large plant needing constant repairs, alterations and improvements, in order to keep the property in a state of efficiency and to enable it to continue a going concern and to earn the interest on the mortgage debt, he intends that the mortgagor shall care for the mortgaged property and make the necessary and proper repairs required to keep the ship or the railroad or whatever it is a going concern. It is always so understood by all the parties concerned ; the mortgagee, the mortgagor and the materialman. In other words, the mortgagee practically makes the mortgagor his agent to take care of the property and to create thereon whatever liens may be necessary to preserve it in an efficient state, and is therefore bound by any such lien and must pay the same before he can take either the *corpus* of the property or the income thereof.

SECOND. The benefit rendered by the materialman is

to the property itself. As is readily apparent, such benefit enures to the mortgagee quite as much as it does to the mortgagor. If the mortgagor cannot take advantage of another man's work, materials and money put into his property without payment, why should not the same equitable principle apply to the mortgagee? If the owner cannot stand by and see money or materials incorporated into and made part of his property, and the same saved from destruction thereby, without the payment for such money and materials becoming a charge upon the property because of the benefit accruing to him therefrom, it would seem as if the mortgagee, who has made the owner his agent to take care of such property, must be equally bound, and unable to take advantage of that which preserved his property without paying therefor.

As we understand it, the only element which it is necessary to find in a case of this character, in order to make the lien of a materialman a preferred claim to a prior mortgage, is that the repairs and materials furnished were necessary in order to keep the property a going concern. That is to say, all cases of repairs might not create a claim ahead of the mortgage. Take the case of a mortgaged hack, which was the property involved in a decision by Mr. Justice GRAY, hereafter referred to. If the mortgagor had rubber tires put upon the wheels, it might be said that the mortgagee never authorized the mortgagor to create a lien upon the hack for any such purpose, as it was not a necessity in order to keep the hack a "going concern," but if the spokes of the wheel were broken in some street collision and the mortgagor had them repaired, it would seem as if the materialman's lien would be preferred to the mortgage for the reason that the repairs were absolutely necessary in order to keep the hack "a going concern" and save the property from becoming a worthless wreck. In other words, the moment it appears that the materials furnished were necessary in order to save the property mort-

gaged and keep it a going concern, that moment the mortgagee is presumed as a matter of law to have authorized the mortgagor to incur the expense of procuring them, and the lien arising from such purchase against the mortgagor is to be preferred to the lien of the prior mortgage for the reasons we have heretofore stated.

In *Hammond vs. Danielson*, 126 Mass., 294, the plaintiff, the mortgagee of a hack, brought a replevin suit to recover possession of the hack from the defendants, who had made repairs thereon at the request of the mortgagor. The defendants claimed to have a lien upon the hack which entitled them to preference over the prior mortgage. Mr. Justice GRAY, then sitting on the Supreme Bench of Massachusetts, sustained the claim and said (at p. 296) :

“ The subject of the mortgage is a hack—that is to say, a carriage let for hire ; described in the mortgage as ‘ now in use ’ at certain stables ; and which, as the parties have agreed in the case stated, the mortgagor retained possession of and used agreeably to the terms of the mortgage. It was the manifest intention of the parties that the hack should continue to be driven for hire, and should be kept in a proper state of repair for that purpose, not merely for the benefit of the mortgagee [mortgagor], but for that of the mortgagor [mortgagee] also, by preserving the value of the security and affording a means of earning wherewithal to pay off the mortgage debt. The case is analogous to those in which courts of common law, as well as of admiralty, have held, upon general principles, independently of any provision of statute, that liens for repairs made by mechanics upon vessels in their possession take precedence of prior mortgages.”

Tucker vs. Werner, 49 N. Y. State Reporter, 571, was a similar case to that just cited. The plaintiff brought a

replevin suit to recover the possession of a buggy upon which he held a mortgage. The defendant claimed that he should first be paid the value of the repairs he had made upon the buggy and that he had a lien therefor ahead of the prior mortgage. The Court held that defendant clearly had a lien against the mortgagor and that the mortgagor, being left in possession of the buggy, was impliedly authorized by the mortgagee to keep it in repair and that defendant's lien had precedence of the mortgage. The Court said at page 572 :

" It may also be assumed, from the nature of the repairs, as shown by the bill, and the character of the property, in constant use, that such repairs were necessary, *useful for its preservation* and enhanced its value. If we are right in these inferences, we have a case where the mortgagee authorized a use of the property, clothed the mortgagor with apparent ownership, and where the work done has added value to the property."

Thereafter in discussing and approving the case of *Hammond vs. Danielson (supra)*, decided by Mr. Justice GRAY, which had been stated by counsel to be unsound, the Court made the following not uninteresting remarks at page 574 :

" It is claimed that this decision is not sound and has in fact been overruled. Its unsoundness is claimed to exist in the fact that it applies to the case the doctrine of maritime liens, but the basis upon which maritime liens are upheld grows out of the fact that they are essential to the preservation of the vessel, that it may be used in the prosecution of its voyage, thus earning money with which to pay the mortgage debt, and also the difficulty of procuring needed repairs in a foreign port, unless the vessel were the pledge of payment, relieved from

other burdens. But what difference in principle can there be where a carriage is used for the purpose of earning money to pay a debt *and the repairs are essential for the preservation and the continuance of earning power?* The article may be the very thing which earns the money, like the hack, or it may be a vehicle by which the individual is enabled to carry on an industry from which he earns what he is obligated to pay. In either event is always found some one of the principles upon which the lien rests, and sometimes they are combined, as where the repairs have added value to the property and thereby enhanced the security, *or the repairs have preserved the property to enable it to pay the security."*

The arguments and reasons which support the creating of a lien in admiralty for supplies furnished a ship which enabled her to continue a "going concern," complete her voyage and reach her home port, would seem to apply with equal force to supplies furnished a railroad which preserve its property, keep it on its feet and enable it to continue a "going concern." The reasons being the same in each case it would seem as if the rule should be the same, without regard to the fact that the questions arise in different branches of the law. Equity and Admiralty are, however, governed by much the same principles in their broad treatment of such a question as is here presented, and the former is not averse to borrowing its reasons and its rules from the latter.

The plaintiff in *Scott vs. Delahunt*, 65 N. Y., 128, brought an action to foreclose a lien for repairs upon a canal boat. The owner and the mortgagees of the boat were made defendants. The mortgagees alone defended. The owner had purchased the boat subject to the mortgage and was running her as master and owner when she foundered and sank and required re-

pairs to put her in condition for navigation. It was held that the lien of the materialman was to be preferred to the mortgage and it was said in the opinion at page 130 :

“ Under such circumstances I am of opinion that plaintiffs’ lien has priority over defendants’ mortgage. *The mortgagees having allowed the owner to continue in the apparent ownership of the boat, making her a source of profit and a means of earning wherewithal to pay off the mortgage debt, the relation so created by implication entitles the owner to do all that may be necessary to keep her in efficient state for that purpose.* The boat having been damaged and rendered unfit for use, the owner did that which was obviously for the advantage of all parties interested ; he put her into the hands of the plaintiffs to be repaired, and, according to all ordinary usage, they ought to have a right of lien on the boat so that those who are interested in her and who will be benefited by the repairs should not be allowed to take her discharged of the lien. Looking to the rights and interests of the parties generally, it cannot be doubted that it is much to the advantage of the mortgagee in such case that the mortgagor or owner should be held to have power to confer a right of lien on the boat for repairs necessary to keep her fit for navigation.”

In *Williams vs. Allsup*, 10 C. B., N. S., 416, the mortgagor of a vessel was left in possession of her and the mortgagee in no way interfered with her management and control. Repairs upon the ship became necessary and the mortgagor had them made by the defendant. Upon the mortgagor being in default in the payment of interest, the plaintiff (being the mortgagee), on examining into the matter, learned

that the ship was in the hands of the defendant, who was repairing her. The plaintiff demanded possession of the ship. The defendant refused to give her up, unless he was paid for the repairs he had made. The question before the Court was, whether the mortgagee was entitled to the possession of the vessel without paying for the repairs. It was held, that the mortgagee must pay for the repairs before he could have the vessel.

It is to be observed that the lien for repairs was not a maritime lien, but a common-law lien against the mortgagor. The reasoning of the Court proceeded entirely upon the theory that the mortgagor acted as the agent of the mortgagee, and that what was done had benefited the security of the mortgage debt. ERLE, C. J., says at page 426 :

" The mortgagee having allowed the mortgagor to continue in the apparent ownership of the vessel, making it a source of profit and a means of earning wherewithal to pay off the mortgage debt, the relation so created by implication entitles the mortgagor to do all that may be necessary to keep her in an efficient state for that purpose. * * * The vessel has been kept in a state to be available as a security to the mortgagee, by her destruction being prevented by the repairs which the defendant has done to her. * * * It is to be observed that the money expended in repairs adds to the value of the ship."

WILLES, J. (at p. 427), said :

" By the permission of the mortgagees the mortgagor has the use of the vessel. He has, therefore, a right to use her in the way in which vessels are ordinarily used. * * * It seems to me that the case is the same as if the mortgagees had been present when the order for the repairs was given.

To that extent I think the property of the mortgagees is impliedly modified."

In the Canada, 7 Sawy., 173, it was held by Judge DEADY that, upon general principles of law and right, one furnishing supplies to a vessel who has no maritime lien therefor and no lien under any State law is entitled to a preference over the mortgagee of the vessel. He says at page 188 :

" Apart from the provision of the New York Statute preferring the lien of the materialman to that of the mortgage, I think it clear upon general principles of law and right, that it is entitled to such preference. A mortgagor in possession represents the mortgagee, and in contracting debts for necessities is, therefore, authorized to bind his interest in the vessel for their payment, so far as the law gives a lien therefor. *In this respect there is an implied agency between them. Necessaries supplied the vessel through the agency of the mortgagor promote the interest of the mortgagee as well as that of the mortgagor, either by enabling the latter to navigate her and thus earn money to pay the indebtedness due the former, or to preserve her value as a security therefor.*"

It is true that, in the extract from Judge DEADY's decision just quoted, he uses the words "so far as the law gives a lien therefor," but the supplies in the case before him were furnished the vessel in her home port upon the request of the owner, so that there was no maritime lien therefor, and he expressly declares that he is considering the question apart from any lien given by the law of New York, the home port of the vessel. But the law of equity gives an equitable lien and the reasoning of Judge DEADY would seem to be perfectly applicable in the present case.

In *White vs. Smith*, 44 N. J. L., 105, 113, the plaintiff, owner of a wagon, allowed her husband to use it in his

business. It became worn out and the husband had it repaired. The defendant assumed that the husband owned the wagon and charged the repairs to him and refused to deliver the wagon unless his charges were paid. The plaintiff thereupon brought an action of trover and the defendant claimed a lien for the amount of his charges. The defendant's claim was sustained upon the ground that plaintiff had authorized her husband to have the repairs made and the wagon kept in running order. As was said by the Court at the end of a well-considered opinion :

“ I think it clear, on the facts certified by the Court below, that the husband had authority from the wife—implied from the manner in which she permitted the wagon to be used—to have the repairs done ; and, if so, the property became by law subject to a lien for the workman's charges.”

It is not clear just what objection can be raised by the counsel for the respondents to the authorities showing that a lien which displaces the mortgage arises for necessary repairs, etc., to a mortgaged property incurred to preserve the same and keep it a “ going concern,” and it may be argued that in some of the cases cited the liens referred to are common-law liens, and not equitable liens. This may be so, but we do not understand that such an argument is of any importance. The question is : Has any lien been created against the property itself and against the owners of the property ? If so, then it is indifferent whether such lien is an equitable lien or a common-law lien. If the lien against the property is in existence, then, whatever its character, so long as it was for some necessity furnished to save and preserve the property and keep it a “ going concern,” it must be preferred to the prior mortgage. The point in all the decisions was not that the lien mentioned was a *common-law* lien as opposed to an *equitable* lien, but that

the material furnished or work done, from which the lien resulted was something which saved and preserved the property mortgaged and kept it a "going concern."

We, therefore, submit that the furnishing of the rails by the Lackawanna Company to the railway company created a lien in favor of the former company against the railway company and its property, and the income therefrom, and that such lien is to be preferred to the mortgage upon the ground that the mortgage creditors impliedly authorized the railway company to create such lien, and have received the benefit of the rails.

III.

THE MORTGAGE FORECLOSURE CASES INVOLVING THIS QUESTION HERETOFORE DECIDED BY THIS COURT.

It is true that Chief-Justice WAITE, in his opinion in *Fosdick vs. Schall* (*supra*), at page 252, says that "railroad mortgages and the rights of railroad mortgagees are comparatively new in the history of judicial proceedings. They are peculiar in their character and affect peculiar interests," and questions arising under railroad foreclosures are sometimes discussed as if railroad mortgages were *sui generis*, and the rules applicable to ordinary mortgages did not apply to them, and this argument may be urged by the other side to show that the cases to which we have referred have no weight in this discussion.

As we understand it, however, the reasons for the application of this rule are stronger in a railroad case than in any other, because of the character of the property involved. In fact, it was said by Mr. Justice LAMAR in *Wood vs. Guarantee Trust Co.*, 128 U. S., 416, 421, that "*the doctrine of Fosdick vs. Schall has never yet been applied in any case, except that of a railroad.*" The case lays great emphasis on the considera-

tion that a railroad is a peculiar property, of a public nature, and discharging a great public work. There is a broad distinction between such a case and that of a purely private concern. We do not undertake to decide the question here, but only point it out." It would seem, therefore, that cases such as we have cited and relating to "purely private" concerns and interests in which this doctrine has been applied are the strongest kind of authority in the present discussion, and that *a fortiori* the principle would be upheld in a case of a railroad foreclosure. Certainly, the claim now pressed upon the attention of the court in the case at bar is akin to that presented to this court in the old case of Williams vs. Gibbs (*supra*), and is the very same as that asserted before and sustained by this court in the comparatively recent railroad foreclosure case of Union Trust Company vs. Morrison, 125 U. S., 591.

In the Morrison case the railroad company was in an insolvent condition and constantly harassed by suits. The Sheriff threatened to levy upon its rolling stock under an execution issued under a judgment against it in the State Court. To prevent such a result and to keep the railroad company going, a bill was filed in equity to enjoin the plaintiff in the State Court suit from proceeding to the collection of his judgment. An injunction was granted in the suit of the railroad company upon condition that the company should give an injunction bond with sureties for the payment of the judgment if the injunction should be dissolved. Morrison at the request of the railroad executed the injunction bond as surety. He was afterwards sued thereon and a judgment was recovered against him in September, 1880.

Morrison executed the bond as surety on or about the 30th of December, 1874, and in November, 1877, a bill to foreclose the mortgage upon the railroad was filed. After the judgment had been recovered against him as surety, Morrison intervened in the fore-

closure proceedings setting forth the facts just recited and asking to be protected from all the consequences of signing the bond upon the ground that by so signing the bond he had protected and preserved the property of the railroad company, and enabled it to continue a "going concern." The position taken by Morrison is stated in the words of Judge BRADLEY, at page 609 of the opinion, as follows: "THE GROUND OF THE CLAIM IS THAT A PORTION OF THE PROPERTY COVERED BY THE MORTGAGE, BEING IN PERIL OF ABSTRACTION AND LOSS, WAS RESCUED AND SAVED TO THE MORTGAGEE BY THE ACT OF THE PETITIONER."

The contention of Morrison was sustained by this Court, as establishing an equitable lien superior to the mortgage, for the reason that his act had saved the property for the mortgagee, and that the latter could not take his money and the direct benefit of the property saved and the indirect benefit of the railroad continuing as a going concern without reimbursing Morrison for the consequences of his act, done in behalf of the mortgagor, and at its request. The Court said, at page 609:

"It [the rolling stock] could have been taken, and this would necessarily have disturbed, and perhaps interrupted, the operations of the railroad, by separating the property seized from the corpus of the estate. The trustees of the mortgage might have prevented such a catastrophe, it is true, by filing a bill of foreclosure and for an injunction and Receiver; but they did not choose to take this course until nearly three years afterwards; on the contrary, they allowed the railroad company to continue to use the property, and to take care of it for them, and stood by and saw Morrison (who had no interest in the matter) put his hands into the fire and rescue the rolling stock of which they were to receive the benefit—both directly, by receiving the property itself without

contest or controversy, and indirectly, by keeping up the railroad as a going concern. Morrison's money, or the fruits of it, has gone into their pockets. And, in this regard, we make no distinction between the mortgagees, the bondholders, whom they represented, the nominal purchasers Horsey and Canda, or the present company. They were all one and the same in interest. If the property became justly affected by the equity of the petitioner's claim, it remains so affected in the hands of the present company." * * *

We respectfully submit that in the Morrison case this Court has recognized that the doctrine for which we contend is applicable to railroad foreclosure suits, and has directly approved the principle that an equitable lien superior to the mortgage arises whenever services are rendered which result in the saving and preserving the mortgaged property and keeping it a "going concern."

How infinitely stronger the equity in the present case is to that found in the Morrison case is quickly apparent from a comparison of the two cases. In the case at bar the rails not only accomplished the purpose of enabling the railway company to continue in business, but they actually became part, and a most important part, of the property itself, which has passed into the hands of the mortgagee, and also put money into the hands of the receivers as the result of the sale of the old rails replaced by those bought of the Lackawanna Company. In the Morrison case the result of the act of Morrison was simply to enable the railroad company to continue in business, and the services rendered by him did not result in the incorporation of anything into the property of the railroad company to be afterwards turned over into the hands of the mortgage creditors and their Receiver. In other words, Morrison, by signing the injunction bond and paying the judgment recovered against him,

simply placed the railroad in a position to continue in business, but in the case at bar the Lackawanna Company, by the sale of the rails, not only enabled the company to keep on as a "going concern," but directly added to the plant to the benefit of the mortgagee.

In *Burnham vs. Bowen*, 111 U. S., 776, the intervenor Bowen filed a petition in a foreclosure suit setting up that prior to the appointment of the Receiver therein coal had been furnished by the Northern Illinois Coal and Iron Company to the Chicago, Dubuque and Minnesota Railroad Company for running its locomotives, and asking that a judgment might be rendered in his favor against the railroad company for the payment of the amount due and that such judgment be declared a lien upon the property and road of the railroad company.

The coal was furnished in 1874 (the exact date does not appear), and the Receiver of the road appointed in the original foreclosure suit brought in the State court, and afterwards removed into the Federal court, was appointed in the month of January, 1875. A decree was entered in favor of the intervenor allowing his claim and directing a sale of the property if the claim was not paid. From this decree an appeal was taken to this Court, and the decree affirmed. In the course of the opinion of the Court, delivered by Mr. Chief-Justice WAITE, it was said at page 780 :

"In our opinion the view which the Circuit Court took of this case was the correct one. The company had never paid its bonded interest. From the very beginning it was in default in this particular, yet the mortgage trustees suffered it to keep possession and manage the property. The maintenance of the road and the prosecution of its business were essential to the preservation of the security of the bondholders. The business of every railroad company is necessarily done more

or less on credit, all parties understanding that current expenses are to be paid out of current earnings. * * *

"The business of a railroad should be treated by a court of equity, under such circumstances, as a 'going concern,' not to be embarrassed by any unnecessary interference with the relations of those who are engaged in or affected by it. * * *

*"The debt due Bowen was incurred to keep the road running, and thus preserve the security of the bond creditors. If the trustees had taken possession under the mortgage, they would have been subjected to similar expenses to do what the company, with their consent and approbation, was doing for them. * * **

"So far as anything appears on the record, the failure of the company to pay the debt to Bowen was due alone to the fact that the expenses of running the road and preserving the security of the bondholders were greater than the receipts from the business. Under these circumstances, we think the debt was a charge in equity on the continuing income, as well that which came into the hands of the court after the receiver was appointed as that before. When, therefore, the court took the earnings of the receivership and applied them to the payment of the fixed charges on the railroad structures, thus increasing the security of the bondholders at the expense of the labor and supply creditors, there was such a diversion of what is denominated in *Fosdick vs. Schall* the 'current debt fund,' as to make it proper to require the mortgagees to pay it back. So far as current expense creditors are concerned, the court should use the income of the receivership in the way the company would have been bound in equity and good conscience to use it if no change in the possession had been made."

The same important difference between the Morrison

case and the case at bar, to which we adverted in the consideration of the Morrison case, also exists between the Burnham case and the present case. The supplies furnished in the Burnham case were coal. It was presumably consumed before the Receiver of the railroad was appointed. Its only advantage and purpose and use, so far as the benefit to the railroad was concerned, was to keep it a "going concern." In the case now under consideration, the Houston and Texas Central Railway Company not only was kept a "going concern" by the rails supplied by the Lackawanna, but such rails became a permanent part of the roadbed and plant of the railway company, which was used by the Receiver, and we do not understand that the equity arising in favor of the materialman because he has kept the railway company a "going concern" by virtue of his supplies is in any way weakened by the fact that such supplies are in fact a permanent improvement of the railroad and are used by the Receiver in the conduct of its business.

The Burnham case as we read it was decided by this Court in exact accord with the doctrine of the cases other than railroad foreclosures to which we have referred the Court. That is to say, the ground of the decision was that the intervenor had an equitable lien for the coal against the railroad company because it preserved the property and kept it a "going concern," and that such lien was to be preferred to the prior mortgage for the reason that the mortgagee had practically made the railroad company its agent to create such lien. These may not have been the exact words used by this Court, but no other inference is to be drawn from the following sentence in the decision, "*the debt due Bowen was incurred to keep the road running and thus preserve the security of the bond creditors. If the trustees had taken possession under the mortgage, they would have been subjected to similar expenses to do what the company, with their consent and approbation, was doing for them.*"

In *Louisville, &c., Railroad Co. vs. Wilson*, 138 U. S., 501, the facts were these : The intervenor, Bluford Wilson, performed services as attorney for the Louisville, Evansville and St. Louis Railroad Company prior to the appointment of its receiver, and part of such service was rendered more than six months prior thereto. The service consisted in the recovery from the Illinois Midland Railway Company of certain engines leased to said company by the Louisville, Evansville and St. Louis Railway Company, and the rentals for their use. The allowance secured by Wilson was \$1,500, and of this amount \$1,340.13 was paid to the receivers of the Louisville, etc., Railway Company. Wilson claimed that his services were worth \$300 and the claim was allowed. This court affirmed the decree below in this respect upon the ground that the bondholders had been benefited by the service and ought to pay for it. Unless there is some material distinction, which does not occur to us, between furnishing brains and furnishing rails to a railway company, we do not see why this case is not a very strong authority in support of our position. In the opinion at page 506 the Court said :

“ The only testimony as to the value of such service fixed it at \$300. Part of such service was rendered more than six months prior to the appointment of a receiver in this case ; but, apparently, the important part within such time. *This recovery inured to the benefit of the security holders, as placing so much more money in the hands of the receiver for the purpose of discharging obligations against the company payable before the bonds. We think it may fairly be held that the party who takes the benefit of such a service ought to pay for it ; and that equity may properly decree payment therefor.*”

In *Union Trust Co. vs. Souther*, 107 U. S., 591, the

appellee intervened in the suit brought to foreclose the mortgage upon the Cairo and St. Louis Railroad Company, claiming that he should be paid for supplies furnished the railroad company prior to the appointment of the Receiver. The character of the supplies is not stated in the report of the case. The Court below directed the payment of the claim and its decision was affirmed by this Court, which said at page 594, after referring to certain paragraphs in *Fosdick vs. Schall (supra)*:

“To this we adhere, and, in our opinion, the right to impose terms does not depend alone on whether current earnings have been used to pay the mortgage debt, principal or interest, instead of current expenses (*Miltenerberger vs. Logansport Railway Company*, 106 *Id.*, 286). Many other circumstances may make such an order reasonable, and this case furnishes a striking example. The first default in the payment of interest under the mortgage occurred in October, 1873. *The bondholders did not see fit to take possession, as they had the right to do, when the default had continued for six months. On the contrary, notwithstanding no payments of interest had been made, they allowed the company to operate the road and incur obligations therefor until December, 1877. This was evidently in the hope that their condition would be improved by the delay; for to effect the forbearance they established an agency and incurred expenses to an amount much larger than the \$3,000 reimbursed by the company. Prior to the appointment of the receiver the gross earnings do not appear to have been enough to pay expenses, but afterwards they yielded a very considerable surplus. There cannot be a doubt that it was for the interest of the bondholders that the road should be kept in operation, and as they did not see fit to take possession while it could only be operated*

at a loss, it was certainly not an abuse of judicial discretion for the court to order, as a condition of granting their application for a receiver, that debts incurred by the company in thus protecting the security should be paid from the income of the receivership, if, in consequence of an increase of revenue, it could be done."

The reason of this decision seems to be that the bondholders "did not see fit to take possession" of the property, but left it in the hands of the mortgagor to be run by it in the usual way in which the operating affairs of a railroad company are carried on, and that the mortgagee having left the mortgagor in possession must be deemed to have authorized it to incur debts in the care of the property and that "debts incurred by the company in thus protecting the security should be paid from the income of the receivership."

The principle which we think should be applied in this case was referred to with approval in *Miltenberger vs. Logansport Railway Co.*, 106 U. S., 286, 311, where it was said by Mr. Justice BLATCHFORD:

"It cannot be affirmed that no items which accrued before the appointment of a Receiver can be allowed in any case. Many circumstances may exist which may make it necessary and indispensable to the business of the road and the preservation of the property for the Receiver to pay pre-existing debts of certain classes, out of the earnings of the receivership, or even the *corpus* of the property, under the order of the Court, with a priority of lien. * * *

"In case of non-payment [of debts] the general consequence involving largely, also, the interests and accommodation of travel and traffic, may well place such payments in the category of payments to preserve the mortgage property in a large sense, by maintaining the good-will and integrity of the

enterprise, and entitle them to be made a first lien"
(p. 312).

The doctrine that supplies furnished to a railroad, which save and preserve the property and keep it a "going concern," are to be paid ahead of the mortgage upon the ground that the mortgagee, by leaving the mortgagor in possession, impliedly authorized him to take care of the property, and to charge it with an equitable lien for any supplies furnished which were necessary in order to continue the road in operation and enable it to earn money to pay its mortgage debt, was again recognized and approved by this Court in the late case of *V. & A. Coal Co. vs. Central Railroad, &c., Co.*, 170 U. S., 355, the material facts in which were as follows :

The coal company had furnished coal to the Richmond and Danville Railroad Company for use upon the lines of the Central Railroad and Banking Company, of Georgia, which were under the control and management of the Danville Company. The contract was dated July 13th, 1891, and the time specified therein for the delivery of the coal was from July 1st, 1891; to July 1st, 1892. In March, 1892, a suit was commenced in the United States Circuit Court in Georgia to cancel the lease of the property of the Central Company to the Georgia Pacific Company and for other specific relief, and a Receiver was appointed upon the 4th of March, 1892. In this suit the coal company intervened and stated in its petition that the "coal was furnished to the Central Company for the purpose of being used by it in the running of its machinery and the prosecution of its business; that a great portion of said coal remained on hand in the bins and storage places of the Central Company at the time of the appointment of the temporary Receiver, and a large portion was still on hand when the Board of Receivers was appointed, and went into possession of said Receivers, and had since that time been actually used by the Receivers in the running of the machinery of, and

the operation of the business of, the Central Company", (p. 359).

After considerable litigation it was eventually decided by the Circuit Court of Appeals for the Fifth Circuit that the coal company was entitled to be paid the amounts due it "for coal delivered to the lines under the control and forming a part of the system of the Central Railroad and Banking Company of Georgia, as shown by the evidence in this cause, including the coal furnished before the appointment of the Receivers and that found in the bins of the line after such appointment, and of which the Receivers took possession."

The decision of the Circuit Court of Appeals was affirmed by this Court, and Mr. Justice WHITE, who delivered the opinion of the Court, after referring with approval to the decisions of *Burnham vs. Bowen*, 111 U. S., 776, and *Miltenberger vs. Logansport Railway Company*, 106 U. S., 286, said at page 367 :

"Is there any good reason why the equitable doctrine, applied in the cases to which we have referred, should not be applied under a state of facts such as shown at bar, where the immediate management of a road was confided by its owners, without protest or interference by the bondholders, to third parties? It would seem not. The dominant feature of the doctrine, as applied in *Burnham vs. Bowen*, is that where expenditures have been made which were essentially necessary to enable the road to be operated as a continuing business, and it was the expectation of the creditors that the indebtedness created would be paid out of the current earnings of the company, a superior equity arises in favor of the materialman as against the mortgage bonds in the income arising both before and after the appointment of a receiver from the operation of the property.

"The equity thus held to arise when a purchase

of necessary current supplies is made by the owning company, is not in anywise influenced by the fact that the company itself is the purchaser of the supplies, but is solely dependent upon the fact that the supplies are sold and purchased for use, and that they are used in the operation of the road, that they are essential for such operation, and that the sale was not made simply upon personal credit, but upon the tacit or express understanding that the current earnings would be appropriated for the payment of the debt. Clearly, if the owning company had entered into an agreement with some individual to commit to his uncontrolled management as their agent the operation of the company's lines, the bondholders could not be heard to say that thereby no equities could arise in favor of labor or supply claimants in the income of the property preserved or kept in operation by their efforts."

It is to be noticed that in the case just referred to the Court went one step further in the matter of agency than is required in the present case. In the Virginia Coal Company case it was held that the mortgagee was bound by the equitable lien created by the lessee of the mortgagor and that such lien was entitled to preference over the mortgage for the reason that the bondholders "without protest or interference" had allowed the owner to place the immediate management of the road in the hands of third parties. In the case at bar the lien was created by the Houston and Texas Central Railway Company, the mortgagor, which had been left in possession of the road and was therefore impliedly authorized to carry it on in a proper manner and in the usual way.

We know of no case in this Court which in any way conflicts with the principle which we now maintain and no decision which seeks to limit the doctrine as announced in *Fosdick vs. Schall*. It has been

sometimes said that the two cases of *Kneeland vs. American Loan Co.*, 136 U. S., 89, and *Thomas vs. Western Car Company*, 149 U. S., 95, were intended by this Court to limit the expression of opinion to be found in *Fosdick vs. Schall*, but as we understand the *Kneeland* and *Thomas* cases, they merely affirm what was the actual decision in *Fosdick vs. Schall* and express no opinion either for or against the so-called doctrine of that case. The facts in *Fosdick vs. Schall*, in the *Kneeland* case and in the *Thomas* case were essentially the same. In each the intervenor claimed payment for the rental of cars prior to the appointment of a Receiver, and in each case the intervenor had retained a vendor's lien upon the cars and had, therefore, apparently not relied upon any equitable lien for the enforcement of his rights under his contract with the railroad company. In each case the cars were returned to the intervenor or declared not to be within the lien of the mortgage, but the rental therefor, which was substantially the purchase price, was held not to be preferred to the mortgage. The contracts for the rental of these cars were in form leases, but were in fact contracts of sale and the so-called rentals were payments on account of purchase price, "with the right to retake possession on default in payment" (*Kneeland* case, 136 U. S., 89, 96).

The distinction between a car-rental case and the case at bar is too obvious for argument. The intervenor in the car-rental cases expressly protected himself by taking a specific lien upon his property and was able to retake it if the purchase money therefor was not paid. By reserving a specific lien upon the property at the time it was sold (which has always been preferred to the prior mortgage), he clearly indicated that he did not rely upon the intervention of a court of equity. It was also hardly to be expected that a court of equity would both return him his property, which he had furnished to the railroad, and then pay him for it also, which would have been the practical

result if such an intervention had been allowed. In other words, the cars were held not to be within the lien of the mortgage and the materialman was permitted to retake them. To allow him to take the cars and to then pay him for their value would have amounted to a double payment, for which there would seem to have been no equitable ground.

In any event it was apparently never intended by this court to limit the doctrine of *Fosdick vs. Schall* by these two decisions, for it was said by Mr. Justice WHITE in the *Coal Company* case (*supra*) at p. 371 that :

“ In neither the *Kneeland* nor the *Thomas* case was there any intention to question the prior decisions of the court, which allowed priority to claims based upon the furnishing of essential and necessary current supplies, not sold upon mere personal credit, against the surplus income arising during the operation of the road under the direction of a court of equity.”

In leaving this point we ask the same question which was asked by Mr. Justice WHITE in the *Coal Company* case at page 367, and respectfully submit that it would seem as if it should receive the answer which he gave thereto. This question, with a slight change made by us, shown by the italics, was :

“ Is there any good reason why the equitable doctrine applied in the cases to which we have referred should not be applied under a state of facts such as shown at bar, where the immediate management of a road was confided * * * without protest or interference by the bondholders to the railway company ? ”

IV.

THE PUBLIC HAVE AN INTEREST IN A RAILROAD, AND ANY REPAIR THEREOF WHICH TENDS TO PRESERVE SUCH PUBLIC INTEREST IS ENTITLED, BECAUSE OF ITS PUBLIC BENEFIT, TO A PREFERENCE OVER A PRIOR MORTGAGE.

The argument that a mortgagee, who leaves the mortgagor in possession of property, is deemed to have made the mortgagor his agent to carry on the property, and to create any lien thereon which may be necessary to keep it a "going concern," is far stronger in the case of a railroad company than in the case of a private concern because of the character of the property and the interest which the public has therein. The great value of a railroad company is, of course, its franchise, and in this the public has an interest, and, on account of this interest of the public, the courts have held that anything furnished to a railroad which keeps it a "going concern," and tends to enable it to retain its franchise must, because of the rights of the public which are thereby preserved, be entitled to be preferred to all private prior rights such as arise from the lien of a prior mortgage.

In *Barton vs. Barbour*, 104 U. S., 126, 135, the interest of the public in a railroad was referred to by this court as follows :

"The cessation of business for a day would be a public injury. A railroad is authorized to be constructed more for the public good to be subserved than for private gain. As a highway for public transportation, it is a matter of public concern, and its construction and management belong primarily to the Commonwealth, and are only put into private hands to subserve the public convenience and economy. But the public retain rights of vast consequence in the road and its appendages, with which neither the company nor any creditor or mortgagee can interfere. *They take*

their rights subject to the rights of the public, and must be content to enjoy them in subordination thereto. It is, therefore, a matter of public right by which the courts, when they take possession of the property, authorize the receiver or other officer in whose charge it is placed to carry on in the usual way those active operations for which it was designed and constructed, so that the public may not suffer detriment by the non-user of the franchises."

In *Olcott vs. The Supervisors*, 16 Wall., 678, 694, it was said :

"The railroads, though constructed by private corporations and owned by them, are public highways, has been the doctrine of nearly all the courts ever since such conveniences for passage and transportation have had any existence. * * * What else does this doctrine mean if not that building a railroad, though it be built by a private corporation, is an act done for a public use? And the reason why the use has always been held a public one is that such a road is a highway whether made by the government itself or by the agency of corporate bodies, or even by individuals when they obtain their power to construct it from legislative grant. * * *

"Whether the use of a railroad is a public or a private one depends in no measure upon the question who constructed it or who owns it. It has never been considered a matter of any importance that the road was built by the agency of a private corporation. No matter who is the agent, the function performed is that of the State. Though the ownership is private, the use is public."

In *Joy vs. St. Louis*, 138 U. S., 1, 47, the public character of a railroad was spoken of by Mr. Justice BLATCHFORD, as follows :

"Considerations of the interests of the public are held to be controlling upon a court of equity, when a public means of transportation, such as a railroad, comes into the possession and under the dominion of the court."

And again he said, at page 50 :

"Railroads are common carriers and owe duties to the public. The rights of the public in respect to these great highways of communication should be fostered by the courts; and it is one of the most useful functions of a court of equity that its methods of procedure are capable of being made such as to accommodate themselves to the development of the interests of the public, in the progress of trade and traffic, by new methods of intercourse and transportation (p. 50)."

The doctrine for which we contend in this case—to wit : that the lien for necessary supplies furnished to a railroad is superior to the lien of a prior mortgage for reasons of public policy has been and is constantly recognized by the courts in the administration of a railroad property when in the hands of its receiver. For supplies furnished to a railroad to keep it a "going concern" after the appointment of a receiver, the courts issue Receiver's certificates, and allow such certificates preference over the prior mortgage in the suit to foreclose which the Receiver was appointed.

In *Wallace vs. Loomis*, 97 U. S., 146, the doctrine of receiver's certificates issued to raise money for the preservation of the property in the hands of a Receiver was declared by Mr. Justice BRADLEY, at page 162, as follows :

"The receivers were authorized by the order appointing them, amongst other things, to put the road in repair and operate the same, and to procure such rolling stock as might be necessary ;

and, for these purposes, to raise money by loan to an amount named in the order, and issue their certificates of indebtedness therefor; and the order declared that such loan should be a first lien on the property, payable before the first mortgage bonds. The power of a court of equity to appoint managing receivers of such property as a railroad, when taken under its charge as a trust fund for the payment of incumbrances, *and to authorize such receivers to raise money necessary for the preservation and management of the property*, and make the same chargeable as a lien thereon for its repayment, cannot, at this day, be seriously disputed. It is a part of that jurisdiction, always exercised by the court, by which it is its duty to protect and preserve the trust funds in its hands."

In *Kneeland vs. Luce*, 141 U. S., 491, 509, the court said:

"Under all the circumstances of the case, the bondholders are precluded from claiming priority over the receiver's certificates, *which were issued for the purpose of preserving the mortgaged property*."

The close analogy between the principle that receiver's certificates for repairs necessary to keep up a railroad are always to be preferred to a prior mortgage, and the doctrine which we maintain, viz.: that such repairs prior to a receivership must also be preferred, because of the public character of the property and the interests of the people therein is well brought out in the case of the *Union Trust Company vs. Illinois Midland Company*, 117 U. S., 434, 462. Among other questions decided by this case, it was held that receiver's certificates for work necessary "in order to place the railway in a suitable condition for the safe transportation of business" were to be preferred to a prior

mortgage and the decision was based upon the cases of Fosdick vs. Schall (*supra*) and Burnham vs. Bowen (*supra*). The great similarity between the facts in the present case and the portion of the Union Trust Company case just referred to is apparent at a glance. In both the repairs were of a worn out road in order to make it safe for traffic. The court said at page 462 :

“ An affidavit annexed to the petition, made by the roadmaster of the Illinois Midland Company, states that, *in order to place the railway in a suitable condition for the safe transportation of business, the expenditure contemplated was absolutely necessary.* The commissioner finds that the money was expended in substantial compliance with the order of the court and that the improvements made by the receiver no more than made up for the deterioration of the road, *especially in view of its imperfect construction and inferior material from the beginning.* This finding was approved by the Circuit Court.

“ As to the certificates of the 18th series issued to replace earnings diverted from paying for operating expenses and ordinary repairs, to pay for betterments, while debts to a large amount had been incurred for the operating expenses and ordinary repairs, it appears by the petition of the receiver and the affidavit of the roadmaster annexed to it, on which the order of June 29, 1881, under which the certificates were issued, was made, that the expenditures for new side tracks and betterments so paid for out of earnings consisted principally of expenditures for roadbed, bridges, iron and ties, *which were in a worn out and insufficient condition.*

“ The commissioner and the Circuit Court rested the allowance of these certificates on what was said by this court in the case of Fosdick vs. Schall, 99 U. S., 235, 273, 254, which views were

applied in *Burnham vs. Bowen*, 111 U. S., 776, to the effect that, when the current income of a railroad in the hands of a receiver is diverted to the improvement of the property by the receiver, and debts for operating expenses are not paid, provision should be made, in foreclosing a mortgage on the road, to pay such debts out of the proceeds of the sale of the property."

It would seem, therefore, that the lien of the petitioners in the present case should be preferred to the lien of the prior mortgage upon the railway company's property not only upon the grounds stated in the authorities other than railroad cases to which we have called the attention of the court, but also because of the special doctrine invoked in railroad foreclosure suits; viz., that the public have an interest in the property superior to any rights of mortgagees, and that any work upon or repair to the property which was required to preserve such public right was entitled to be paid out of the income or out of the *corpus* of the property prior to the payment of any prior mortgage thereon.

V.

IT WILL SUFFICE FOR THE PURPOSES OF THIS CASE TO RECOGNIZE THE LIEN AS TO INCOME.

We have heretofore argued this case as if the question was whether upon the facts presented therein the petitioners have a lien upon the corpus of the property of the railway company, but it is a somewhat larger and broader question than necessarily arises here, for the fund now in court upon which the petitioners claim a lien and which is sufficient to pay their claim is the income earned by the railway company while in the hands of receivers and earned by reason and by the use of the rails furnished by the Lackawanna Company to the railway company.

Further than that it is to be observed that after these rails were furnished by the Lackawanna Company just prior to the failure of the railway company large sums of money far exceeding in amount this claim were diverted from the income and used to pay dividends to the holders of Waco and Northwestern Division First Mortgage Bonds and for the improvement of the mortgaged property.

When due weight is given to these considerations and to the fact that the circuit court has always with great care provided in every decree in the various litigations referred to in the statement of this case that such decree was to be without prejudice to the rights of these petitioners as against the income of the railway company it is very evident that the position of the petitioners as to such income is even stronger and more within the remedial power of a court of equity than their claim against the *corpus* of the property of the railway company.

This was the view of this Court in the case of *Fosdick vs. Schall*, 99 U. S., 235, when Chief-Justice WAITE in considering the question whether an "order for the payment out of the fund in court of the rent of the cars during the time they were used by the receivers, appointed by the State Court, and for six months before, [was] justifiable under the circumstances of the case," said at pages 251 *et seq.* :

"As to the second question, we have no doubt that, when a court of chancery is asked by railroad mortgagees to appoint a receiver of railroad property pending proceedings for foreclosure, the court, in the exercise of a sound judicial discretion, may, as a condition of issuing the necessary order, impose such terms, in reference to the payment from the income during the receivership of outstanding debts for labor, supplies, equipment, or permanent improvement of the mortgaged property, as may, under the circumstances of the particular

case, appear to be reasonable. Railroad mortgages and the rights of railroad mortgagees are comparatively new in the history of judicial proceedings. They are peculiar in their character and affect peculiar interests. The amounts involved are generally large, and the rights of the parties oftentimes complicated and conflicting. It rarely happens that a foreclosure is carried through to the end without some concessions by some parties from their strict legal rights, in order to secure advantages that could not otherwise be attained, and which it is supposed will operate for the general good of all who are interested. This results almost as a matter of necessity from the peculiar circumstances which surround such litigation.

“ The business of all railroad companies is done to a greater or less extent on credit. This credit is longer or shorter, as the necessities of the case require ; and, when companies become pecuniarily embarrassed, it frequently happens that debts for labor, supplies, equipment and improvements are permitted to accumulate, in order that bonded interest may be paid and a disastrous foreclosure postponed, if not altogether avoided. In this way the daily and monthly earnings which ordinarily should go to pay the daily and monthly expenses are kept from those to whom in equity they belong, and used to pay the mortgage debt. The income out of which the mortgagee is to be paid is the net income obtained by deducting from the gross earnings what is required for necessary operating and managing expenses, proper equipment and useful improvements. Every railroad mortgagee in accepting his security impliedly agrees that the current debts made in the ordinary course of business shall be paid from the current receipts before he has any claim upon the income. If, for the convenience of the moment, something is taken from what may not improperly be called the

current debt fund, and put into that which belongs to the mortgage creditors, it certainly is not inequitable for the court, when asked by the mortgagees to take possession of the future income and hold it for their benefit, to require as a condition of such an order that what is due from the earnings to the current debt shall be paid by the court from the future current receipts before anything derived from that source goes to the mortgagees. In this way the court will only do what if a receiver should not be appointed the company ought itself to do. For even though the mortgage may in terms give a lien upon the profits and income, until possession of the mortgaged premises is actually taken or something equivalent done, the whole earnings belong to the company and are subject to its control (*Galveston Railroad vs. Cowdrey*, 11 Wall., 459; *Gilman et al. vs. Illinois and Mississippi Telegraph Co.*, 91 U. S., 603; *American Bridge Co. vs. Heidelberg*, 94 Id., 798).

"The mortgagee has his strict rights, which he may enforce in the ordinary way. If he asks no favors, he need grant none. But, if he calls upon a court of chancery to put forth its extraordinary powers and grant him purely equitable relief, he may with propriety be required to submit to the operation of a rule which always applies in such cases, and do equity in order to get equity. The appointment of a receiver is not a matter of strict right. Such an application always calls for the exercise of judicial discretion; and the Chancellor should so mold his order that, while favoring one, injustice is not done to another. If this cannot be accomplished, the application should ordinarily be denied.

"We think, also, that if no such order is made when the receiver is appointed, and it appears in the progress of the cause that bonded interest has

been paid, additional equipment provided, or lasting and valuable improvements made out of earnings which ought in equity to have been employed to keep down debts for labor, supplies and the like, it is within the power of the court to use the income of the receivership to discharge obligations which, but for the diversion of funds, would have been paid in the ordinary course of business. This, not because the creditors to whom such debts are due have in law a lien upon the mortgaged property or the income, but because, in a sense, the officers of the company are trustees of the earnings for the benefit of the different classes of creditors and the stockholders; and, if they give to one class of creditors that which properly belongs to another, the court may, upon an adjustment of the accounts, so use the income which comes into its own hands, as if practicable, to restore the parties to their original equitable rights. While, ordinarily, this power is confined to the appropriation of the income of the receivership and the proceeds of moneyed assets that have been taken from the company, cases may arise where equity will require the use of the proceeds of the sale of the mortgaged property in the same way. Thus, it often happens that, in the course of the administration of the cause, the court is called upon to take income which would otherwise be applied to the payment of old debts for current expenses, and use it to make permanent improvements on the fixed property, or to buy additional equipment. In this way the value of the mortgaged property is not unfrequently materially increased. It is not to be supposed that any such use of the income will be directed by the court, without giving the parties in interest an opportunity to be heard against it. Generally, as we know, both from observation and experience, all such orders are made at the request of the par-

ties, or with their consent. Under such circumstances, it is easy to see that there may sometimes be a propriety in paying back to the income from the proceeds of the sale what is thus again diverted from the current-debt fund in order to increase the value of the property sold. The same may sometimes be true in respect to expenditures before the receivership. No fixed and inflexible rule can be laid down for the government of the courts in all cases. Each case will necessarily have its own peculiarities, which must be a greater or less extent influence the Chancellor when he comes to act. The power rests upon the fact that in the administration of the affairs of the company the mortgage creditors have got possession of that which in equity belonged to the whole or a part of the general creditors. Whatever is done, therefore, must be with a view to a restoration by the mortgage creditors of that which they have thus inequitably obtained. It follows that if there has been in reality no diversion, there can be no restoration, and that the amount of restoration should be made to depend upon the amount of the diversion. If in the exercise of this power errors are committed, they, like others, are open to correction on appeal. All depends upon a proper application of well-settled rules of equity jurisprudence to the facts of the case as established by the evidence."

VI.

THE RIGHT OF A MATERIALMAN TO BE PAID FOR SUPPLIES FURNISHED BY HIM TO KEEP A RAILROAD A "GOING CONCERN" IS NOT DETERMINED BY THE TIME WHEN THE SUPPLIES WERE FURNISHED PRIOR TO THE APPOINTMENT OF THE RECEIVER IN FORECLOSURE PROCEEDINGS.

The rails were delivered to the railway company by the Lackawanna Company in February, March, April

and May, 1884, and the first Receivers were appointed in February, 1885, so that less than one year intervened between the time of delivery of the rails and the appointment of Receivers. The petition of intervention of the Lackawanna Company was first filed on the 12th day of September, 1885.

That such a lapse of time is not considered a bar to an equitable lien of this nature is shown by the following cases :

In *Hale vs. Frost*, 99 U. S., 389, some of the supplies furnished by the intervenor Hale, Ayer & Co. were apparently delivered to the railway company as early as 1872. The Receiver was appointed in the foreclosure proceedings in May, 1875.

In *Burnham vs. Bowen*, 111 U. S., 776, the coal was delivered in the year 1874, but the precise time in the year does not appear. The Receivers were appointed in January, 1875.

In *Union Trust Co. vs. Morrison*, 125 U. S., 591, the injunction bond, the signing of which saved the railroad and kept it in existence, was executed in 1874 and the Receiver was not appointed until November, 1877.

In *Louisville, &c., Railroad Co. vs. Wilson*, 138 U. S., 501, part of the services were rendered more than six months before the appointment of the Receiver.

In *V. & A. Coal Co. vs. Central Railroad, &c., Co.*, 170 U. S., 355, the coal was delivered in monthly installments beginning July 1st, 1891, and the Receiver was appointed in March, 1892.

It will be observed from the statement of facts that ever since the Lackawanna Company filed its intervention in cause No. 185 on the 12th day of September, 1885, it has at all times had an intervention pending involving the rails delivered to the railway company under the contracts hereinbefore referred to in the matter of the Receivership of the Waco and Northwestern Division of the Railway Company in every phase which that litigation has assumed. It is also to be noticed that the Receivership ordered in Consoli-

dated Cause No. 198 has been continued concurrently with the Receivership in cause No. 227 down to the present time. Any intimation, therefore, of laches or that the Lackawanna Company has slept upon its rights is entirely disproved.

SECOND POINT.

The Farmers' Loan and Trust Company and the beneficiaries under its trust had no lien upon any of the earnings of the Waco and Northwestern Division of the Houston and Texas Central Railway Company which were collected by the Receivers in Causes Nos. 185 and 198 prior to the filing of the foreclosure bill in Cause No. 227. An amount of said earnings far more than sufficient to pay the claim of the Lackawanna Company was diverted under orders of court from the payment of current-income creditors to the payment of mortgage creditors, or to the improvement of the mortgaged property. The current-income fund, to the extent to which it was so depleted, will be restored out of the proceeds of sale of the mortgaged property, or out of the income now in the hands of the court.

Inasmuch as the allowance of a claim of the character of the one set up by the Lackawanna Company is one resting so largely in the discretion of the

Chancellor, it is important to show the nature of any conflicting claims upon the revenues of the defendant Railway Company, because if no conflicting claims exist, or if the conflicting claims be of a character not commending themselves to the Chancellor, they may be disregarded in the exercise of the judicial discretion allowed in such cases. That the mortgagee, under this mortgage had no mortgage upon income, is seen from a mere inspection of the mortgage (Rec., p. 14).

In the case of United States Trust Company vs. Wabash Railway, 150 U. S., 287, 306, where the mortgage did not cover income and was apparently in its terms similar to the mortgage in the present case, it was held that the mortgagee had no claim to income earned prior to its taking possession of the railway company's property. The court, speaking through Mr. Justice BROWN, said at page 306 :

"There is another reason, however, why the Trust Company is not entitled to the rental of this property prior to demanding possession thereof in its bill of foreclosure. The petition avers that, by reason of the defaults in the payment of the rentals, the receivers 'are indebted to your petitioner for the use and occupation of the said demised premises under the said lease.' But the mortgage or deed of trust to the Trust Company, the petitioner, did not purport to convey any of the incomes or earnings of the road, but provided that if default should, at any time, occur in the payment of interest, the trustee should, when requested so to do, take possession of the mortgaged property and operate the same and collect and receive all the tolls and income thereof. It was also provided that, until such default, the mortgagors should be entitled to have and to hold the possession of the railroad, and collect, receive and retain all the revenues arising from its use. * * *

"Now, if the mortgage had covered the earnings and rentals of the property, and those had constituted a part of the estate conveyed to the Trust Company as security for the bonds there would be some reason for saying that it would be entitled to recover these earnings and rentals in this action before it demanded possession of the road. But where the mortgage provides that the mortgagor shall remain in possession until default, but when default occurs the trustee may enter, this court has held that the trustee can only secure the earnings of the mortgaged property by taking or demanding possession."

Even if this mortgage had been a mortgage upon income, it would have given no lien upon the earnings of the road while it remained in the hands of the Company.

Railroad Co. vs. Cowdrey, 11 Wall., 459.

Smith vs. Railroad, 124 Mass., 154.

Gilman vs. Telegraph Company, 91 U. S., 603.

American Bridge Co. vs. Heidelbach, 94 U. S., 798.

The lien of a mortgage upon the earnings of a railroad depends solely upon its terms, and until the trustee takes some step authorized by the mortgage to appropriate the earnings no lien attaches to them.

Miltenberger vs. Logansport Railway Co., 106 U. S., 286, 307.

We quote passages from several of the decisions of this court stating the circumstances which determine the respective rights of the mortgagor and the mortgagee to the income of the property mortgaged.

In *Dow vs. Railroad Company*, 124 U. S., 652, this court stated the respective rights of the parties as follows at page 654 :

"It is well settled that the mortgagor of a railroad, even though the mortgage covers income, cannot be required to account to the mortgagee for earnings while the property remains in his possession until a demand has been made on him therefor, or for a surrender of the possession under the provisions of the mortgage."

In concluding the opinion, at page 656, it is further said :

"Under these circumstance, *as there are no current expense creditors claiming the fund*" (italics ours) "we are satisfied that the money is to be treated as income covered by the mortgages, and should be paid to the trustees, to be held as part of that security."

The case of *Sage vs. Memphis & Little Rock R. R. Co.*, 125 U. S., 361, seems to us absolutely indistinguishable in principle from our case.

In that case a judgment creditor of the defendant company obtained the appointment of a receiver; that receiver was subsequently discharged, but only after a large amount of revenues had accumulated in his hands, which he was ordered to hold, subject to the orders of the court appointing him. Trustees of a mortgage of the railways of the defendant company, after the discharge of the receiver, and whilst he still held the income in his hands, filed a foreclosure bill, and also intervened in Sage's suit, claiming the income in the hands of the receiver. The Circuit Court recognized the claim and rejected Sage's demand to be paid out of said income. This Court reversed the decision of the lower court and ordered Sage to be paid in full.

In this case we have an exact duplicate of the *Sage* case, except that the income has been expended by the court for the benefit of the mortgage bondholders. That fact cannot affect the identity of principle between the two cases for two reasons ; viz. :

(1) Because *actus curiæ neminem gravabit* is a general principle of law ; and

(2) Because the court expressly reserved the rights of the Lackawanna Company in every order and decree which it rendered using the income ; so that the rights of that Company stand to-day just as they stood on September 12th, 1885, when it first intervened in the Southern Development Company Receivership (*i. e.*, Receivership in 185).

The Sage case is so exact a counterpart of our own that almost every line of the decision in that cause is applicable here. We nevertheless quote from it as follows at page 378 :

“ The trustees filed their bill of foreclosure June 26, 1883, but they did not intervene as trustees in this suit until February 23, 1884, some time after the discharge of the receiver and after the property had been surrendered to the company. Their claim and intervention shows upon its face that no part of the interest accruing upon the bonds secured by their mortgage subsequent to January 1, 1882, had been paid at the time they so intervened. By the terms of that mortgage it was provided that, in case of continuous default by the railroad company for thirty days after maturity in paying any of the sums specified in the interest coupons, the principal sums in all the bonds ‘ shall immediately become due and payable,’ and thereupon the trustees, upon the written request of the holders of a majority of said bonds, ‘ shall enter upon and take possession of all and singular the charter, franchises and property hereby conveyed, and shall and may sell the same to the highest bidder for cash in hand,’ etc. There was no moment pending the receivership when these trustees, upon the request of the holders of a majority of the bonds, might not have appeared in this suit, or in a separate suit in the same court,

and asked that the receiver hold for them as well as Sage, or that he be discharged and they put in possession of the mortgaged property, for the purposes of sale, pursuant to the mortgage. Neither they nor the bondholders elected to pursue that course. It may be that their action was dictated in part by the fact, found by the master, that the railroad, the principal security for their debts, was being largely improved during the receivership out of the income of the property, and that no part of that income was being diverted to pay Sage's judgment or the debts of the Company. If the trustees, pending the receivership, had intervened and asked possession of the property, they might perhaps have been entitled, as against general creditors, to the income of the property thereafter accruing, upon the principles announced by this court in *Dow vs. Memphis and Little Rock Railroad Co. (as reorganized)*, 124 U. S., 652. But we do not perceive any legal ground upon which they are entitled to the net earnings of the property, while it was in the hands of the receiver, in a suit instituted by a judgment creditor for the protection of his own interests, and not of the interests of the trustees, or of the bondholders, or of other creditors. His suit was, in effect, an equitable levy for his benefit, upon the net income of the property. Other creditors who filed their claims, based upon judgments, gain nothing, as between themselves and Sage, by the fact that their judgments were rendered upon coupons which were secured by lien upon the mortgaged property. Neither they nor their trustees, prior to the termination of the receivership, chose to assert this lien. Nor did they, pending the receivership, ask that the receiver should from and after their appearance hold for them as well as for Sage. They took action as simple contract creditors, whose

claims were reduced to judgment. If the bondholders, when intervening simply as judgment creditors, acquired an interest in the fund, they could not, upon any recognized principles of equity, deprive the creditor at whose instance and for whose benefit the receiver was appointed of his priority of right arising from the institution of suit for the purpose of reaching the income of the debtor's property. The judgments at law obtained by bondholders upon their coupons were all rendered after the receiver took possession of the property; some in the Spring of 1883, the larger part of them in October and November of that year, just before the receiver was discharged."

The action of the trustees, and of the bondholders in the Sage case, and in the Lackawanna case was identical.

Turning backward in the examination of the authorities we find *Kountze vs. Omaha Hotel Company*, 107 U. S., 378, *et seq.*, to be a most instructive case upon the principles now before the court for adjudication.

The *Kountze* case was an action on an appeal bond given for *superseatas* of execution on a decree of foreclosure rendered by the Circuit Court for the District of Nebraska, and the question was as to the measure of damages to be recovered on the bond. In determining this question it was necessary to determine whether or not the plaintiffs were entitled to recover rents and profits or damages for the use and detention, as it is otherwise called.

Upon this branch of the case Judge BRADLEY, in 107 U. S., 392, *et seq.*, said:

"And yet there is a material difference between the case of ejectment and a suit for the foreclosure of a mortgage.

"The difference is this: In ejectment the property of the land is in question, and if the

plaintiff has the right he is entitled to immediate possession, and to the perception of the rents and profits, which belong to him, and for which the defendant in possession is accountable to him. Every dollar, or dollar's worth, is so much of the plaintiff's property of which he is deprived. And the same is true in dower. But in the case of a mortgage the land is in the nature of a pledge, and it is only the land itself—the specific thing—which is pledged. The rents and profits are not pledged; they belong to the tenant in possession, whether the mortgagor or a third person claiming under him. This is not only the common law, but it is the express statute law of Nebraska, which declares that, 'in the absence of stipulations to the contrary, the mortgagor retains the legal title and right of possession.' The plaintiff in this case was not entitled to possession, nor to the rents and profits. His foreclosure suit did not seek possession, but sought the sale of a specific thing—the land. In such a case, until the litigation is ended, it doth not appear that there must be a sale, or even that the plaintiff is entitled to a sale. The defendant in possession is entitled to redeem the land until a sale is made, and until then he is entitled to the rents and profits which belong to him as of right. The taking of the rents and profits prior to the sale does not injure the mortgagee, for the simple reason that they do not belong to him. Waste—that is, destruction or injury to the land itself, as before stated—is an injury to the mortgagee. It diminishes the value of the pledge, and for such injury no doubt he might recover on the appeal bond. Other deteriorations, such as occur by want of repairs, accumulation of taxes, fires not covered by reasonable insurance, and the like, probably might also be fairly covered by the bond. But perception of rents and profits is the mortgagor's right

until a final determination of the right to sell, and a sale made accordingly."

See, also, *Teal vs. Walker*, 111 U. S., 242, where the Court, after announcing the general doctrine, further holds, that the case against the right of the mortgagee to recover rents and profits before foreclosure, is strengthened by the provisions of the General Statutes of the State of Oregon, to the effect that a mortgage of real property shall not be deemed a conveyance so as to enable the owner of the mortgage to recover possession of the real property without a foreclosure and sale according to law.

The laws of Texas are exactly the same upon this subject as those of the State of Oregon.

Article 1,340 of the Revised Statutes of Texas (see 1 Sayles' Texas Civil Statutes, p. 447) provides that :

"Judgments for the foreclosure of mortgages and other liens shall be, that the plaintiff recover his debt, damages and costs, with a foreclosure of the plaintiff's lien on the property subject thereto, and * * * that an order of sale shall issue to the sheriff or any constable of the county where such property may be, directing him to seize and sell the same as under execution, in satisfaction of the judgment, etc."

The Supreme Court of Texas, by a long line of decisions, the most noteworthy of which is the case of *Duty vs. Graham*, 12 Texas, 427, has expressly decided that, under this statute and under the laws of the State of Texas, a mortgage is a mere security for the payment of a debt. The mortgagor remains the real owner of the land and entitled to its possession, and the mortgagee cannot sustain an action of trespass to try title or ejectment against the mortgagor on the mortgage.

In the latest case decided by the Supreme Court of

Texas on this subject (*Giles vs. Stanton*, 86 Texas, 620, 627) the Court says:

“The Mortgagees under this mortgage had no lien upon the earnings of the road while it remained in the hands of the company. * * * The lien of the mortgage upon the earnings of the railway depended solely upon the terms of the mortgage, and until the trustee took some steps authorized by the mortgage to appropriate the earnings no lien attached to the earnings. * * * By the terms of the mortgage the company was to remain in possession of the road, and had the right to operate the same, and to appropriate the earnings and income. Upon default in the payment of interest continuing for six months, the trustee was empowered to take possession of the railway, and operate it, applying the net earnings to the satisfaction of the interest, or he might sue to foreclose the mortgage, and if such default continued for twelve months the trustee was authorized to sue to foreclose the mortgage. The trustee did not demand nor take possession of the road, and took no steps towards foreclosing the mortgage until the 18th day of June, 1891, when the plea of intervention was filed. It follows that the lien of the mortgage did not attach to the earnings of the road in the hands of the receiver which were earned before the date of the filing of the intervention, but from that time the lien of the mortgage attached to such earnings, subject to the expenditures and claims which by law were given a preference over it.”

By the terms of the mortgage sued upon in this cause, the Houston and Texas Central Railway Company was to remain in possession of its property, and had the right to operate the same and appropriate earnings and income until default, continuing for the time

stipulated in the mortgage, in which event the trustee was empowered to take possession of the railroad and operate it, applying net earnings to the satisfaction of interest. The trustee not only failed to take possession of the road, but never until it filed its foreclosure bill in Cause No. 227, took any steps whatsoever to assert any lien upon the earnings.

The provision of the mortgage that the trustee should take possession is, however, as above shown, absolutely worthless, under the laws of the State of Texas.

We, therefore, respectfully submit that the Farmers' Loan and Trust Company has never had the slightest title to the rents and revenues of the property of the defendant corporation, either before or since the filing of its bill of foreclosure in this cause, and we, therefore, conclude that the petitioners are the only persons before the Court having any claim to the income in question.

THIRD POINT.

If neither the Farmers' Loan and Trust Company nor the Lackawanna Company had any lien upon the earnings of the Waco and Northwestern Division of the Houston and Texas Central Railway Company collected by the Receivers in Causes 185 and 198 before the filing of the foreclosure bill in Cause No. 227, then that income should be distributed ratably between all the creditors of the railway company, and the Court, having diverted the earnings in question and devoted them

to the payment of the mortgage creditors or to the improvement of the mortgaged property, will, after reconstituting the current income fund to the extent to which it has been depleted, distribute the same ratably among the creditors of the defendant railway company now before the court—to wit, between the Farmers' Loan and Trust Company and the Lackawanna Iron and Coal Company.

If this court should conclude that the amount collected by the Receivers in causes 185 and 198 should be prorated between the creditors of the railway company who are parties to this cause, then it would seem that such distribution should be not upon the full amount of the mortgage debt, but upon the amount of the mortgage debt less the sum received by the bondholders upon the foreclosure sale of the property. That is to say, the basis of distribution to the mortgage creditors should be the amount of the deficiency judgment against the railway company at the foreclosure sale.

The principle of distribution which should control in this regard is that declared in *Wheeler vs. Walton & Whann Co.*, 72 Fed. Rep., 966, 967, where it was said :

“ Under an assignment for the benefit of creditors, which is virtually the case now before the court, a creditor holding notes of third persons as collateral security, by collecting those notes before a dividend is made, *must credit the amount collected upon the principal debt, and take a dividend upon the remainder only of the debt.* He cannot collect the collaterals and then claim a dividend upon the principal debt as it was at the time of the assignment.”

We do not know that the rule found in some cases in the lower federal courts that a creditor of an insolvent debtor cannot be required, in proving his claim, to allow credit for any collateral securities which he may hold, has any application to the present case. The situation here is that there is a fund in court to be equitably distributed between two claimants, and the question for the court to determine is what is the amount of each claim at the time the distribution of the money is to be made. In other words, the distribution of the fund in court is not to relate back and be as of the date of the first insolvency of the railway company, but is to be made upon the facts as they exist at the present time. That is to say, the mortgage creditors, having received a large part of their mortgage debt and being in fact only claimants of this fund to the amount which they failed to realize from the sale of the property are entitled to be paid a dividend only upon the amount of the deficiency judgment obtained by them.

Even if the rule that a creditor is not required to allow for collateral when proving his claim against an insolvent did have anything to do with the case at bar, it would seem that to pay the mortgage creditors a dividend upon the deficiency judgment only was the true and proper application of such rule, for, as we understand it, the meaning of the rule simply is that the claim proved, and upon which a dividend should be paid, must be the amount due the creditor at the time of the insolvency, which amount is, of course, not affected by any collateral held by such creditor. If before insolvency of his debtor the creditor had realized upon collateral held by him, he would obviously not be permitted to prove the amount of his claim without allowing credit for the collateral theretofore collected by him. In the case suggested the time for the determination of the amount of the claim dates from the act of insolvency, so here the time for the determination of the amount of the claims against this fund is

at the date of the distribution. Prior to that time the mortgage creditors received a large sum upon their mortgage debt. This sum should be credited upon their claim, and any dividend coming to them from the fund in court should, as it seems to us, be distributed upon the basis of their original mortgage debt, less whatever they have heretofore received on account thereof.

In determining this question it must not be forgotten that the court is seeking to make an *equitable* distribution of the money in its hands.

FOURTH POINT.

The Farmers' Loan and Trust Company and the beneficiaries under its trust have no lien upon the earnings of the Waco and Northwestern Division of the Railway Company which have been collected by the Receiver since the filing of the bill by said Trust Company in Cause 227 (present cause).

The mere filing of the bill of foreclosure in Cause 227, and the appointment of a Receiver therein, did not of itself create a lien in favor of the complainant upon all income thereafter earned by the property involved in such suit. As we understand it, the result, and the only result, of filing the bill and appointing the Receiver in Cause 227 was to place the property, and any income therefrom, in the custody of the court, to be by it equitably dealt with.

This was substantially the decision of this court in

Porter vs. Sabin, 149 U. S., 473, 479, where it was said by Mr. Justice GRAY, that,

“ When a court exercising jurisdiction in equity appoints a receiver of all the property of a corporation, the court assumes the administration of the estate ; the possession of the receiver is the possession of the court ; and the court itself holds and administers the estate, through the receiver as its officer, for the benefit of those whom the court shall ultimately adjudge to be entitled to it.”

In the case of Quincy, &c., Railroad Co. vs. Humphreys, 145 U. S., 82, 97, Mr. Chief-Justice FULLER stated the rule as follows :

“ They [the receivers] were ministerial officers appointed by the Court of Chancery to take possession of and preserve *pendente lite* the fund or property in litigation ; mere custodians, coming within the rule stated in Chicago Union Bank vs. Kansas City Bank, 136 U. S., 223, 236, where this court said : ‘ A receiver derives his authority from the act of the court appointing him, and not from the act of the parties at whose suggestion or by whose consent he is appointed ; and the utmost effect of his appointment is to put the property from that time into his custody as an officer of the court, for the benefit of the party ultimately proved to be entitled, but not to change the title or even the right of possession in the property.’ ”

In Davis vs. Gray, 16 Wall., 203, 217, the court held that :

“ A receiver is appointed upon a principle of justice for the benefit of all concerned. Every kind of property of such a nature that, if legal, it might be taken in execution, may, if equitable, be put into his possession. Hence the appoint-

ment has been said to be an equitable execution. He is virtually a representative of the court, and of all the parties in interest in the litigation wherein he is appointed. He is required to take possession of property as directed, because it is deemed more for the interests of justice that he should do so than that the property should be in the possession of either of the parties in the litigation. *He is not appointed for the benefit of either of the parties, but of all concerned. Money or property in his hands is in custodia legis.*"

Perhaps as good a discussion of this question as can be found in the reports is in the Virginia case of *Beverly vs. Brooke*, 4 Grat., 187, 208, where the court said :

" By means of the appointment of a receiver a Court of Equity takes possession of the property which is the subject of the suit, preserves it from waste or destruction, secures and collects the proceeds or profits, and ultimately disposes of them according to the rights and priorities of those entitled, whether regular parties in the cause or only parties in interest coming before the court in a seasonable time, and due course of proceeding, to assert and establish their pretensions. * * *

" The order of appointment is in the nature, not of an attachment, but a sequestration ; *it gives in itself no advantage to the party applying for it over other claimants.*"

The force of this argument would seem to be all the stronger when it is remembered that the mortgage in the present cause was not a mortgage of income, but simply of the corpus of the property of the railway company. Whatever may be the rule as to the effect upon the income of a railway property resulting from the filing of a bill to foreclose a mortgage which, by

its terms, is a mortgage of income, it would seem to be clear that, in the present case, where there is no mortgage of income, the mere filing of the bill to foreclose such mortgage cannot create a lien upon anything which was not covered by and included within the terms of such mortgage.

FIFTH POINT.

If the Farmers' Loan and Trust Company has no specific lien upon the earnings of the Waco and Northwestern Division of the Railway Company collected by the Receiver appointed upon the filing of the bill in Cause No. 227, then such earnings should be paid to the petitioners or should be ratably distributed between the petitioners and the Farmers' Loan and Trust Company.

If we are right in our position that the mere filing of a bill in a foreclosure suit does not confer a specific lien in favor of the complainant therein upon the income of the property involved in such suit (and we think we are), then the question which presents itself is which of the two claimants of the income earned in Cause No. 227 has the greater equity therein. Is it the Lackawanna Company, which a few months prior to the failure of the railway company furnished to it rails which were laid upon 30 miles out of 58 of the property foreclosed and which have earned the fund in court or is it the Trust Company, which has simply filed a foreclosure bill? It would seem as if the party who has furnished the rails which earned

the money in court had a claim thereon which was entitled to recognition before any claim arising from the mere filing a bill and placing the property in the hands of a receiver.

If, however, a superior claim to the fund in court arises in favor of the party who brings the property into the custody of the court by filing a foreclosure bill and placing the railway company in the hands of a receiver, then such superior equity in favor of the Lackawanna Company and prior in point of time to any such claim in favor of the Trust Company would seem to result from the intervention petition, which is substantially an ancillary bill, which was filed by the Lackawanna Company in Consolidated Cause No. 198 on the 26th day of November, 1886, and which is still pending and under which the receivership in said Consolidated Cause No. 198 was ordered to be concurrent with the receivership in this Cause No. 227.

It appears, therefore, that the petitioners are entitled to the income earned during the receivership in Cause No. 227 upon the ground (1) that even if neither the Lackawanna Company or the Trust Company have any specific lien upon the fund in court, yet upon the facts the equity in favor of the Lackawanna Company which furnished the rails which earned the money is the greater, and upon the further ground (2) that any priority arising from filing a bill and placing the property in the hands of a receiver appointed by the court is in favor of the Lackawanna Company which first filed its still pending intervention in Consolidated Cause No. 198, in 1886, some years prior to the filing of the bill by the Trust Company in Cause No. 227.

If the claim of the petitioners upon the income collected by the receiver appointed in Cause No. 227 is not entitled for the reasons just stated to be preferred to any claim thereon made by the Trust Company, then the two claims are to be treated as upon an equality, and

the income collected by the Receiver in Cause No. 227 should be ratably divided between them, the Lackawanna Company participating upon the basis of the unpaid bills for rails furnished by it, and the Trust Company participating upon the basis of the portion of the mortgage debt remaining unpaid after application thereto of the proceeds of sale of the corpus of the railway property.

It is not to be overlooked in the consideration of this case that the mortgage creditors have already sold the rails furnished by the Lackawanna Company and still unpaid for, and have by reason of such rails received a largely increased price for the entire property of the Waco and Northwestern Division. The question now before the court is as to a distribution of money earned by these very same rails. Is it equitable that the mortgage creditors should pocket both the money realized from the sale of the rails and the money earned by the rails prior to their sale, and that the Lackawanna Company should go unpaid?

SIXTH POINT.

The claim of the Lackawanna Company should be preferred to the lien of the mortgage involved in this cause or the fund in court distributed ratably among the creditors of the railway company.

E. B. KRUTTSCHNITT,
MAXWELL EVARTS,
Of Counsel for Petitioners.

In the Supreme Court of the United States.
OCTOBER TERM, 1897.

No. _____

LACKAWANNA IRON & COAL CO. ET AL,
PETITIONERS,
VS.
FARMERS' LOAN & TRUST COMPANY, ET AL,
RESPONDENTS.

BRIEF FOR MORAN BROS. AND HENRY K. MCHARG, RE-
SPONDENTS, AND INTERVENING BOND HOLDERS,
IN OPPOSITION TO THE PETITION FOR
WRIT OF CERTIORARI.

We oppose the petition for *certiorari* on three grounds,
as follows :

FIRST. Petitioners' case, as disposed of in the Circuit
Court and Circuit Court of Appeals, is not of the class of

cases that come within any rule announced by this Court in which writs of *certiorari* will be granted.

SECOND. Petitioners' case was disposed of in the Circuit Court and Circuit Court of Appeals on the merits, in accordance with principles repeatedly announced and firmly established by this court in similar cases. In other words, the decision is right on the merits, not in conflict with other Federal Court decisions, and the application should be denied.

THIRD. Petitioner's case was disposed of in the Circuit Court and Circuit Court of Appeals on findings of the special master to the effect that petitioners *sold the rails to the railway company on its general credit*; that the *sale was of an unusually large amount of rail*, and that petitioners' *claim could not be classed as a current debt* made in the ordinary course of business, and said findings are not excepted to by petitioners, and there is no evidence in the record so that such findings may be reviewed by this court.

The facts supporting the three objections are so interwoven and connected we find that all can be conveniently presented together.

While the opinion of the Circuit Court of Appeals reviews the leading cases on the subject of preferential claims, in answer to petitioners' various contentions, the case is made to turn in that court, as it turned before the Master and in the Circuit Court, on questions of fact peculiar to this case. The underlying facts upon which the opinion rests are the following facts found by the Circuit Court of Appeals and the Special Master: (Italics in all quotations ours.)

- (1) That petitioners' claim is for rails that "were sup-

plied, not as a matter arising in the ordinary course of the railroads operations, *but for the virtual reconstruction of the road.*" This finding is fortified by the facts found by the Master, that the railway purchased, under the contracts set up by petitioners, 18,581 tons of rail, which at the prices agreed to, amounted to the sum of \$735,454.30, sufficient rail to lay down new 214 77-100 miles of track, and this entire purchase was made in twelve to fourteen months by a road having only about 500 miles of track. (R. 650 to 655.) (Court's opinion, R. p. —, and 79 Fed. Rep. at top of page 210.) And upon these facts the Court remarks: "No authorities need be cited to establish the proposition that works of reconstruction are not entitled to preferential payment."

(2) "The unusually large purchase of rails; the time within which they were to be delivered; the condition of the road; the contracts providing for notes at six months, renewable for a like term at the makers option; the hypothecation of securities for the payment of the claims; the knowledge which the intervenor had of the mortgage; the fact that the contract contained no promise to pay out of any particular fund; the time which elapsed between the date of the contract and the appointment of the receiver in cause No. 185, are circumstances which, taken together, *cannot fail to convince us that the intervenor relied upon the general credit of the railway company.*" (Court's opinion, R. p. —, and 79 Fed. Rep., p. 210.)

(3) "I find that the debt for which the Lackawanna Company claims payment in its petition, *cannot be classed as a current debt made in the ordinary course of business*, as those terms seem generally to be understood." (Master's finding, R. p. 656.)

(4) "I find that * * * *the credit extended under said contracts was at the request of and for the accommodation of the defendant railway company, and upon its general credit. That said sales were made without any stipulation that security should be given by the defendant company for said rails, or that payment therefor should be made out of any particular fund or in any particular way; said sales were of an unusually large amount of rails, and defendant was unable to pay cash therefor. That petitioner * * * had knowledge of the mortgage," &c. (Master's findings, R. pp. 656 and 657.)*

The foregoing are the facts which have controlled the destiny of this case on its way through all the courts. Summarized, these facts read: The railway company's road was run down, and it bought this unusually large amount of rails for the purpose of virtually reconstructing its road, and not as a matter arising in the ordinary operation of the road. That the rails were bought upon the *general credit of the railway company*, and upon a credit to suit the convenience and accommodation of the railway company, without any agreement that payment should be made in any particular manner, or out of any particular fund, and the claim cannot be classed as a current debt.

These findings stand, and must ever stand, unchallenged, because petitioners furnish no way of attacking them. There are, in the first place, no exceptions addressed to them; and in the second place, if there were any such exceptions, this Court could not test their correctness, for the evidence upon which the Master and Circuit Court acted is not in the record. Petitioners surely cannot ask this Court to attack these findings of fact when they have never done so. But this is not all. The decree of the

Circuit Court shows that that Court passed on the *evidence* as well as the Master's report. (R. p. 681.) The evidence is not here. How can that decree be reviewed without it?

Upon this state of the record can it be contended seriously that any question of general importance or of peculiar gravity can arise out of this sale of general merchandise to a railroad company on its general credit for purposes of general reconstruction by a railroad supply creditor? Can there be a doubt in the mind of a single member of this Court that petitioners' claim was properly denied priority over the mortgage bonds, when it appears, without controversy, to be a claim for general merchandise, sold on the general credit of the railway company for the purpose of virtually reconstructing its road, and cannot be classed as a current debt?

We do not understand that this Court desires to re-examine the grounds on which its decisions rest, which hold that claims for general merchandise for purposes of general construction, are entitled to no preference over prior mortgage bonds. It has never been held, within our knowledge, that such claims have any standing under the doctrine of *Fosdick vs. Scholl*. Will the fact that a claimant asserts that his claim comes within the doctrine of that case, (when he comes here with a claim for general merchandise only) bring his case within the rule of this Court allowing writs of *certiorari*? Can it be seriously contended that this case is one where the decision conflicts with other decisions so that the writ ought to issue "to secure uniformity of decision"? Can there be found in the whole range of cases a single case that gives priority to the character of claim shown by the record in this case?

Counsel for petitioners base their right to a writ of certiorari on the ground, among others, that there is a conflict between this case and that of *Southern Railway Co. vs. Carnegie Steel Company*, and they argue from this assumed, but unestablished conclusion, that the writ prayed for must be granted in the interest of uniformity of decision. A more indefensible position could hardly be taken than to stand for the proposition that this case is like the Carnegie case, or the *Rowena Clark*, the other case cited by petitioners. The comparison instituted in the petitioners' application is simply no comparison whatever. Had as well say that two cases involving the title to two horses are the same in principle because each horse has four legs, two eyes and one tail as to say that the two claims asserted by two different intervenors in separate railway receiverships are the same in principle because "both cases involve two successive receiverships, to-wit: First, a receivership instituted, not at the suit of a mortgagee, but at the instance of other creditors, to protect the property from disruption and to hold it together; and thereafter a supervening receivership, provoked by bondholders, and to which the first receivership was made to account. Both cases involved a claim for steel rails, involved a consideration of the effect to be given to the fact that promissory notes were given in evidence of a credit extended for said rails; involved renewals of the notes so given, and involved the alleged laches of the petitioners." (*Petition for certiorari*, p. 23.) We understand that the distinguishing facts in all cases of this character are: Was the debt contracted upon the general credit of the railway company? Were the supplies purchased for, or used in, the general operation of the road, or were the supplies

purchased as general merchandise, or used for purposes of general construction, or the virtual reconstruction of the road? The facts in this case showing petitioner's claim to be for general merchandise sufficiently appears from what has been said.

We now direct attention to the cases referred to by petitioners. We refer, first, to the Carnegie case. In that case, there are no findings of fact that the purchase was "unusually large in amount," or that the purchase was made for "virtually reconstructing the road" or that the rail was sold on the "general credit" of the railway company, or that the claim could not be classed as a "current debt" made in the usual course of business. On the contrary, it is found by Judges Simonton and Morris, both of whom delivered opinions in that case, that the claim of the Carnegie company was a *current debt*. This fact, that the Carnegie claim was a current debt, together with the further fact that there had been a diversion of the revenue of the road, lay at the very foundation of the case.

A bare reference to the Rowena Clark case will show how different it is to the petitioners' claim. We quote from the opinion stating the nature of the claims in that case. Judge Toumlin, in stating the case, says:

"From what appears in the record we are satisfied that the debts claimed by intervenors for coal delivered prior to the appointment of the receivers were current debts for operating expenses of the Central Railroad lines, made in the ordinary course of business, to be paid out of the current earnings. The coal was purchased in the name of the Central Railroad. It was delivered on its lines and

was furnished for their operation, and with the exception of a small amount was used by them."

In both the Carnegie and Rowena Clark cases, the Circuit Court of Appeals treated the claims as "current debts" contracted in the general operation of the railways. In both cases priority was given the claimants over the mortgaged bonds by the Circuit Court of Appeals, and in both cases at the instance of the railways and other parties adversely interested to the claimants, this honorable court granted writs of certiorari, and that action is cited as a precedent by petitioners, and made the basis and practically the sole ground for the demand that a writ of certiorari be granted in this case, when the claim of petitioners is proven without controversy and treated throughout as a claim for general merchandise, bought for purposes of reconstruction, in an unusually large quantity, and could not be classed as a current debt, and the priority is denied. We judge from the argument and statement of the ground upon which it is asked that the writ of certiorari be granted, that it is supposed this court, having granted writs of certiorari in two cases which involve the rights of claimants seeking priority over mortgage bonds, that the door is thrown wide open—that a general invitation is extended to all who have claims seeking ~~propriety~~ *priority* to apply and the prayer of their petitions will be granted, regardless of merit or the correctness of the decision complained of. Had as well assume that this court, having granted its writ in a patent, admiralty or municipal bond case, will grant writs to all comers who can show a patent, admiralty or municipal bond case. This is the sequence of the logic used to obtain the writ prayed for, or counsel seem to think it is necessary that this court have before it

all cases which may be decided by the Circuit Court of Appeals involving claims of priority over railway mortgage bonds before a decision may be reached in the cases in which writs have already been granted. Such a practice would, if logically pursued, result eventually in bringing to this court every case decided by the Circuit Court of Appeals which involved kindred questions to any case in which a certiorari had been granted. We do not understand from the decisions of this court that such has entered into its remotest conception. The rule, as we understand it, is that each case must stand or fall on its own merits. The case presented must show that it, not some other case, presents a question of "peculiar gravity," or "general importance," or "conflict of decisions," among the Federal Courts. We feel warranted in assuming that this court is entirely satisfied with the decisions in the following well considered cases, in all of which claims of the general class asserted by petitioners were denied priority:

Thomas vs. Car Co., 149 U. S. 95.

Bound vs. Ry. Co., 58 Fed. 473.

Hale vs. Frost, 99 U. S. 389.

Heiderkoper vs. Locomotive Works, 99 U. S. 258.

Wood vs. Guarantee Trust Co., 128 U. S. 416.

Kneeland vs. Trust Co., 136 U. S. 89.

Finance Co. vs. Charleston Ry. Co., 10 C. C. A. 323.
(s. c.) 62 Fed. Rep., 205.

Railroad Co. vs. Hamilton, 134 U. S. 68.

Railway Co. vs. Cowdry, 11 Wall 482. *rely*

Counsel for petitioners also ~~deny~~ on that part of the 6th finding of the special master wherein he reports: "That at the time when the contracts hereinbefore mentioned

were entered into between the Lackawanna Company and the defendant railway company, that the condition of the track of the defendant railway company was such that the demand for new rails upon the most worn portion of the roadway was practically imperative." Further: "The condition of these roads was bad, except such portions as has been relaid with 5000 tons of rails purchased prior to December 28th, 1882. There was continual breakage of rails and wrecking of trains, the track was unsafe and was generally so regarded not only by railroad men but by the traveling public; the damage to merchandise, rolling stock, etc., was continuous and the need for new rails appears to have been almost absolutely necessary as a preservation of human life, the loss of which was liable to occur any moment." (R. p. 565)

This condition of things is relied on as showing that the rails were needed to keep the road a "going concern." The trouble with the petitioners' case is that these facts prove too much, especially when taken in connection with the other findings of the master referred to above—that the purchase was unusually large in amount, and that the debt could not be classed as a current debt. The purchase seems to have been very suddenly made whereby 18,581 tons of rail were purchased in the very short space of from 12 to 14 months, at a cost of \$735,454.30, and which was sufficient in amount to lay down a new track 214.77 miles on the road of a railway company which owned only about 500 miles of road. These facts clearly support the finding of the Circuit Court of Appeals that "the purchase was made to virtually reconstruct the road."

The foregoing discussion precludes the necessity of

giving any special attention to petitioners' claim that the payment of \$91,371.00 interest to the mortgage bondholders in May, 1887, by the receiver in cause No. 198 was a division of funds from petitioners' claim justly applicable to it. But we believe we have two sufficient answers to this claim. In the first place, it must be shown that petitioners' claim is of the preferential class before they can avail themselves of the doctrine of diversion, or, in other words, claim that there has been a diversion. We do not understand that a general creditor who is not protected by the peculiar equity which brings his case within the protection of this court is in a position to complain that other creditors have been paid certain amounts on their debts. In the second place, it appears from the master's findings that the accounts of the receivership were not kept in a manner so that it could be determined out of what fund this payment of interest was made. On this subject the master finds:

"I further find that the accounts of said railway company were not kept in such a manner as to indicate the exact fund out of which the interest on said first mortgage bonds of the Waco & Northwestern Division were paid, or the exact fund out of which the interest upon the bonds of the other divisions was paid." (R. p. 680.)

As to the erection of betterments on the mortgaged premises, the findings are of the same inconclusive nature. The master nowhere finds that any improvements were erected and paid out of the income of the road. He finds on this subject as follows:

"I find that Alfred Abeel, receiver in this cause, has expended under the order of this court, \$46,505.40 for betterments and permanent improvements from Decem-

ber 10th, 1892, to September 3rd, 1895, consisting of bridges, shops and round house, car shed, water stations, locomotives, chair car and fencing."

"I find that no part of the income arising from the operation of the road and no part of the proceeds of sales of old iron, old rails, old cars and engines, which was received by the receivers in causes Nos. 185 and 198, ever came into the possession of the receiver in this cause, and the evidence fails to show that any part of the new equipment purchased by the receivers in causes Nos. 185 and 198, as shown above, ever came into the possession of the receivers in this cause. The evidence fails to show that any improvements and betterments of the property added to the property of the Houston & Texas Central Railway Company by the receivers in causes Nos. 185 and 198, were made on the Waco & Northwestern division." (R. pp. 663 to 664.)

It will be observed that he does not find that these betterments were paid for out of the revenue of the road. The record shows that the mortgage covered a large landed property, aggregating 223,622.28 acres of land, besides vendor's lien notes aggregating \$107,145.66, still on hand, and which has during all this time been in the hands of the receiver. (R. pp. 391 to 441.) For ought that appears, the small amount of improvements erected by Abeel, the present receiver, were made out of funds arising from the sale of lands, or collection of land notes covered by the mortgage. In such case no diversion could exist. At least the burden was on petitioners, not only to allege but to prove a diversion. The Circuit Court of Appeals of the sixth circuit, in the case of Central Trust Co. vs. East Tenn. V. & G. Ry. Co., 80

Fed. at page 626, disposes of a claim that there had been a diversion upon a record substantially similar to the record in this case, and say:

"But it is also shown that, during the same period, money was borrowed on open account, more than sufficient to equal the diversion complained of, which went into a common treasury, from which operating expenses, preferential claims, interest, and improvements were paid, without any definite showing as to whether the borrowed money was applied to the payment of interest and improvements, or to current income debts. Under this system of book-keeping, the addition of borrowed money to the income arising from operation showed a substantial surplus after payment of the great mass of income debts, and all disbursements on account of interest upon the two mortgages foreclosed, as well as upon improvements in the roadway. Prior to the period covered by the maturity of appellant's claims, there was a surplus of gross earnings over all operating expenses; but it cannot be contended that the company was under any obligation to future creditors to accumulate a surplus to meet possible deficiencies in the income to meet future income debts, or that it was improper to apply such surplus in payment of interest. *St Louis A. & T. H. R. Co. vs. Cleveland C. C. & I. Ry. Co.*, 125 U. S. 658-675, 8 Sup. Ct. 1011. Whatever diversion there may have been of income to payment of debts or liabilities, not properly debts of the income, seems to have been more than reimbursed by the money borrowed. *The burden is upon complainants to show that there has been a misappropriation of earnings to the improvement of the mortgaged property, or to the payment of interest, before the mortgagees can be justly called*

upon to reimburse the fund applicable to debts of the income in consequence of such diversion. If interest was paid or improvements made out of borrowed money, then there was no diversion; or if made out of gross earnings, and the latter was reimbursed by borrowed money, the diversion was made good. The abstracts showing income from all sources and disbursements upon all accounts are somewhat complicated, in consequence of the mode of book-keeping adopted. The commissioner and court below concurred in reporting that there was no diversion shown. In the absence of very cogent evidence of mistake of fact, or of some error of the law, the finding of fact by the commissioner must be accepted as final. *Emil Kiewert Co. vs. Juneau*, 24 C. C. A. 294, 78 Fed. 708; *Kimberly vs. Arms*, 129 U. S. 512-524, 9 Sup. Ct. 355; *Tilghman vs. Proctor*, 125 U. S. 136, 8 Sup. Ct. 894; *Turley vs. Turley*, 85 Tenn., 256, 1 S. W. 891."

On what has been said, we are content to leave the case in the hands of this court on the question of diversion.

This brings us to the last inquiry; that is, whether petitioners have shown that they are entitled to have the decree appealed from reversed and the case sent back so that they may demand pro rata division of the income in the hands of the receiver among all the creditors? This proposition is based on the claim that the mortgage bonds are not secured by a lien on the income after possession was taken. The Circuit Court of Appeals of the 5th circuit, on the same day the opinion was delivered in this case, held, in the case of *Geo. E. Downs vs. Farmers' Loan & Trust Company, et al*, that the mortgage in this case did cover the income. (79 Fed. Rep at page 221.)

And petitioners claim is based upon the further contention that no one had a lien on the \$91,371.00 interest paid to the bondholders, and proceeding from that assumption, it is demanded that this money should have been paid on the Lackawanna claim, at least its pro rata.

There is no warrant for the assumption that no one had a lien on the fund that was used in paying interest on the bonds. For the purposes of this point it may be conceded that the interest was paid out of current income as claimed by petitioners. The findings of the master show that on February 16th, 1885, the Southern Development Company filed its original bill of complaint against the Houston & Texas Central Railway Company in cause No. 185, and that upon this bill receivers, Clark and Dillingham, were appointed. That on March 31st, 1885, the Farmers' Loan & Trust Company filed its petition in said cause No. 185, praying to be made a party thereto, averring, among other things, that it was trustee under several separate mortgages executed by defendant railway company, and naming among them the mortgage declared herein. That the prayer of said petition was granted, and on April 6th, 1885, said court entered an order in said cause No. 185, allowing the Farmers' Loan & Trust Company to become a defendant in said suit; and further ordering that it may demur, plead or answer therein on or before the rule day in June, 1885. (R. pp. 671-2.) The record shows that demurrers were filed to the bill of complaint of the Southern Development Company by Easton & Rentool, trustees in one or more of the mortgages executed by defendant railway company, and on May 26th, 1886, these demurrers were in all things sustained, and the entire bill and the supplemental bill of the Southern Develop-

ment Company was dismissed. Upon the dismissal of these bills in cause No. 185, all the property was transferred to receivers in consolidated cause 198. That no other action was thereafter taken in cause 185, but causes 198, 199 and 201 were consolidated, and proceeded to judgment and foreclosure as consolidated cause 198. This consolidation of these causes took place on May 26th, 1886, and the three causes were filed a few months prior to this. (R. p. 672.) The bills in causes 198, 199 and 201 were bills to foreclose three mortgages given by the Houston & Texas Central Railway Company on its railway and properties. One was on the main line, the other on the Austin branch, and the third was a general mortgage on the whole system.

Neither the bills of complaint or the mortgages declared on in causes 198, 199 and 201 are in the record, and for that reason it cannot be determined whether these mortgages, in terms, covered the income after possession was taken. But it is clear that at the suit of the trustees in the mortgages declared on in causes 198, 199 and 201, all the property, income, rents and profits of the Houston & Texas Central Railway was, on May 26th, 1886, placed in the hands of receivers. By placing the property in the hands of receivers the complainants in those bills made an equitable levy upon the rents and profits to accrue from the operation of the road by the receivers. (*Sage vs. Memphis etc. R'y Co.*, 125 U. S., 365.) And it is very likely that the mortgages were drawn in the usual manner of such mortgages, giving a lien on the income after possession is taken. As petitioners failed to bring up with the record these mortgages, it may be assumed that if here they would be of no value to them. It, therefore, appears with rea-

sonable certainty, that there was a lien on the income of the road and the whole system, after possession was taken at the suit of complainants in causes 198, 199 and 201 on May 26th, 1886, and continuously thereafter, and this lien was in favor of the mortgaged bondholders, secured by the mortgages declared on in the above three causes.

The interest payment of \$91,371.00 to the bondholders secured by mortgage on the Waco & Northwestern branch so much complained of, was not made until May 1st, 1887, nearly a year after the receivers appointed in consolidated cause 198 had taken possession. This fact is perfectly manifest from the record. Under these conditions, and while the whole net revenue of the road was under lien to secure the mortgages declared on causes 198, 199 and 201, the complainants in those causes jointly with the trustee in the first mortgage on the Waco & Northwestern branch, applied to the court to have the coupons which matured on January 1st and July 1st, 1885, paid on all the bonds. The prayer of this petition was granted, and the interest was paid on all the first mortgage bonds, and the interest paid to these bondholders amounted to \$91,371.00. As it appears petitioners' claim is not of the preferred class, and as it further appears that the use of the current income for the payment of interest was with the express consent and at the request of the bondholders holding a lien on the very fund used, and who alone could complain, there was certainly no "diversion" of which petitioners could complain. That is patent.

Let us view the matter from another standpoint. Suppose this \$91,371.00 was to-day returned to the receivers in consolidated cause 198, and petitioners should apply to have it divided on the principle that equality is equity, and

demand a *pro rata* distribution? Would its petition be granted? No. Why?

Because they would be shown that the fund was net income which arose by operation of the road by the receivers appointed in consolidated cause 198, and that the bondholders either held a lien on this income by the terms of their mortgages after possession was taken, or by virtue of the equitable levy through the appointment of the receivers, and the whole fund would go the bondholders in those mortgages, and petitioners, after the labor and pains of much hard sailing, would be found stranded upon a barren shore, penniless and forelorn. If the bondholders, secured by mortgages declared on in cause 198, chose to allow and invite the bondholders in this cause to participate in a fund to which they had no legal or equitable right, and which belonged to the bondholders in cause 198, that was a matter which could not concern petitioners. Petitioners were not thereby deprived of a right of any description. They were not thereby made to lose a dollar. Not one dollar of the money that was paid to the Waco & Northwestern bondholders could have been recovered by petitioners, if the interest had not been paid. In a free fight, under the most favorable conditions, the able counsel for petitioners could not hope to successfully engineer this scheme of *ratable* distribution. It is a bare, naked falacy. It is a delusion. This court will not send this case back to the court below to enable counsel to chase a phantom.

We beg to call attention to the fact that this claim for *pro rata* distribution is an afterthought and a makeshift. No mention of such a claim can be found in petitioners' petition of intervention. (R. pp. 616 to 634.) The claim was prosecuted in the lower court upon the demand that

petitioners were entitled to priority over the bondholders. The contest was with the bondholders alone. No other party but these two could have an interest in that controversy. But in the doctrine of general equitable distribution now urged, all the creditors must be brought in and a general adjustment take place. This idea was the first time advanced in the Circuit Court of Appeals on page 24 of petitioners' brief in that court. It had not been, prior to that time, a matter of any concern to petitioners whether the bondholders had a lien or not. They claimed a lien prior and paramount to the best and highest. There is no assignment of error based upon this idea. It is a new tack, based upon the fertile imagination of the able and ingenious counsel who made it, but has no substantial foundation in any issue in this case.

But suppose it be conceded that the fund used to pay the \$91,371 00 interest was not net income, and that nobody had a lien upon or charge against it. This concession aids petitioners not in the least. In the first place there is neither pleading or parties before the court to warrant the relief demanded. But the fatal answer to petitioner's scheme for equitable distribution, by requiring the bondholders to refund the \$91,371.00, and take their share ratably, is that it is nowhere shown that upon the division proposed the bondholders would be entitled to less than they have already gotten. The record shows that the principal of the indebtedness due to these bondholders is over a million dollars. That the bonds bear interest at 7 per cent. per annum. That the only money paid them during a period of over 12 years, from July 1st, 1864, to this date, is the pittance of \$91,371.00, and it is solemnly and earnestly demanded that they be required to return that,

so that petitioners may go back to the lower court and get together all the creditors, find out what each has received on his claim, and have a general division, and this, too, some ten years after the final decree of foreclosure has been entered in consolidated cause 198; the property all sold, and the proceeds distributed to thousands of creditors who are scattered to the four winds of heaven.

But this is not all. If for a moment it were conceded that petitioners ever had the remotest interest in the \$91,371.00 paid on the bonds secured by the mortgage foreclosed herein, and had an apparent right to complain of this payment, we beg to call attention to the manner in which the holders of these bonds were treated by the receiver in causes Nos. 185, 198 and 227, until Alfred Abeel was appointed receiver to succeed Mr. Dillingham in December, 1892. This subject is treated fully in our main brief filed in the Circuit Court of Appeals, (a copy of which is filed herewith) under our fifth proposition, page

Summarized the treatment was this: During the time the entire system of the Houston & Texas Central Railway, which included the Waco branch, was in the hands of receivers from February, 1885, to December, 1892, there was spent in betterments and permanent improvements by the receivers \$763,404.03. Not a dollar of this was put on the Waco branch. That branch is about one ninth in mileage of the entire system, and was justly entitled to one ninth of the betterments, which would be \$84,822.67. It not only received no betterments by the receivers, but the old rail taken up by the company from that branch was on hand when the receivers were appointed, and was by them sold for \$38,480.00 net. The mortgage, without doubt, covered these rails. The

Waco branch is therefore entitled to an equity equal to these two amounts, or the sum of \$123,302.67 in the proposed pro rata distribution. These equities are superior to the claim of any unsecured general creditor like petitioners. This amount must, therefore, be deducted from the imaginary general fund proposed by petitioners and placed to the credit of the Waco branch, and it is only the balance left after this deduction is made that will be subject to the demanded equitable pro rata distribution. This amount would be more than sufficient to pay for all the rails laid down on the Waco branch out of the Lackawanna purchases, as the principal of the sum demanded against that branch is only \$105,547.15, as this amount does not bear interest. (Thomas vs. Car Co., 149 U. S. 95.)

From this showing, we may reasonably conclude that if the demand of petitioners was granted and the case sent back for pro rata distribution, it would avail them nothing. But no question of "peculiar gravity" or "general importance" is raised in the failure of the Circuit Court of Appeals to pass on and consider this claim for equitable pro rata distribution.

If that was a grave and important question, petitioners surely would have raised the point in the Circuit Court. It is a little strange that a right which is so grave and important as to form the subject of a petition for *certiorari* would have been wholly neglected in the prosecution of this case for a period of over 12 years, and was never raised until the idea was incorporated in the brief of petitioners filed in the Circuit Court of Appeals. (See brief, page 24.)

It will be borne in mind, further, that no ground is assigned as a reason why this court should grant the writ and review the action of the Circuit Court of Appeals in failing to pass on the question under discussion. It is nowhere claimed that a question of peculiar gravity, general importance or conflict of decision is involved in that question.

We have now gone over all the grounds insisted on in the petition. We have not seen the brief filed by petitioners' counsel in support of the petition, but we are lead to believe from what we see in the petition that no new point has been raised.

We are advised by the petition that the briefs filed by petitioners in the Circuit Court of Appeals have been filed in this court. We likewise file herewith copies of our briefs filed in the Circuit Court of Appeals as follows:

"Brief for Appellees, Moran Bros. and Henry K. McHarg," which presents the merits of the defense. "Supplemental Brief of Moran Bros. and Henry K. McHarg" which is devoted mainly to correcting errors found in the brief of petitioners, filed in that court. "Brief of Moran Bros. and Henry K. McHarg, Appellees, in Opposition to Motion for Rehearing," which is a reply to the first brief filed by petitioners in support of their motion for rehearing, and an "Additional and Supplemental Brief in Opposition to Rehearing," which is a reply to the last brief filed by petitioners for rehearing. We feel that in view of the fact that petitioners have filed their briefs, we should file ours in reply. And we submit with confidence

that petitioners have shown no reason why this court should grant a writ of *certiorari*, and respectfully ask that the prayer of the petition be denied.

Respectfully submitted,

L. W. CAMPBELL,

Solicitor for Moran Bros. and Henry K. McHarg, Intervening bond holders.

Set No. 22.
last Opp. to By. of Campbell
for Respondent.
451
FILED
JULY 11 1897
JAMES H. MCKENNEY
CLERK

Filed Oct. 16, 1897.

**UNITED STATES CIRCUIT COURT OF APPEALS,
FIFTH CIRCUIT.**

**LACKAWANNA IRON AND COAL COMPANY,
APPELLANT,**

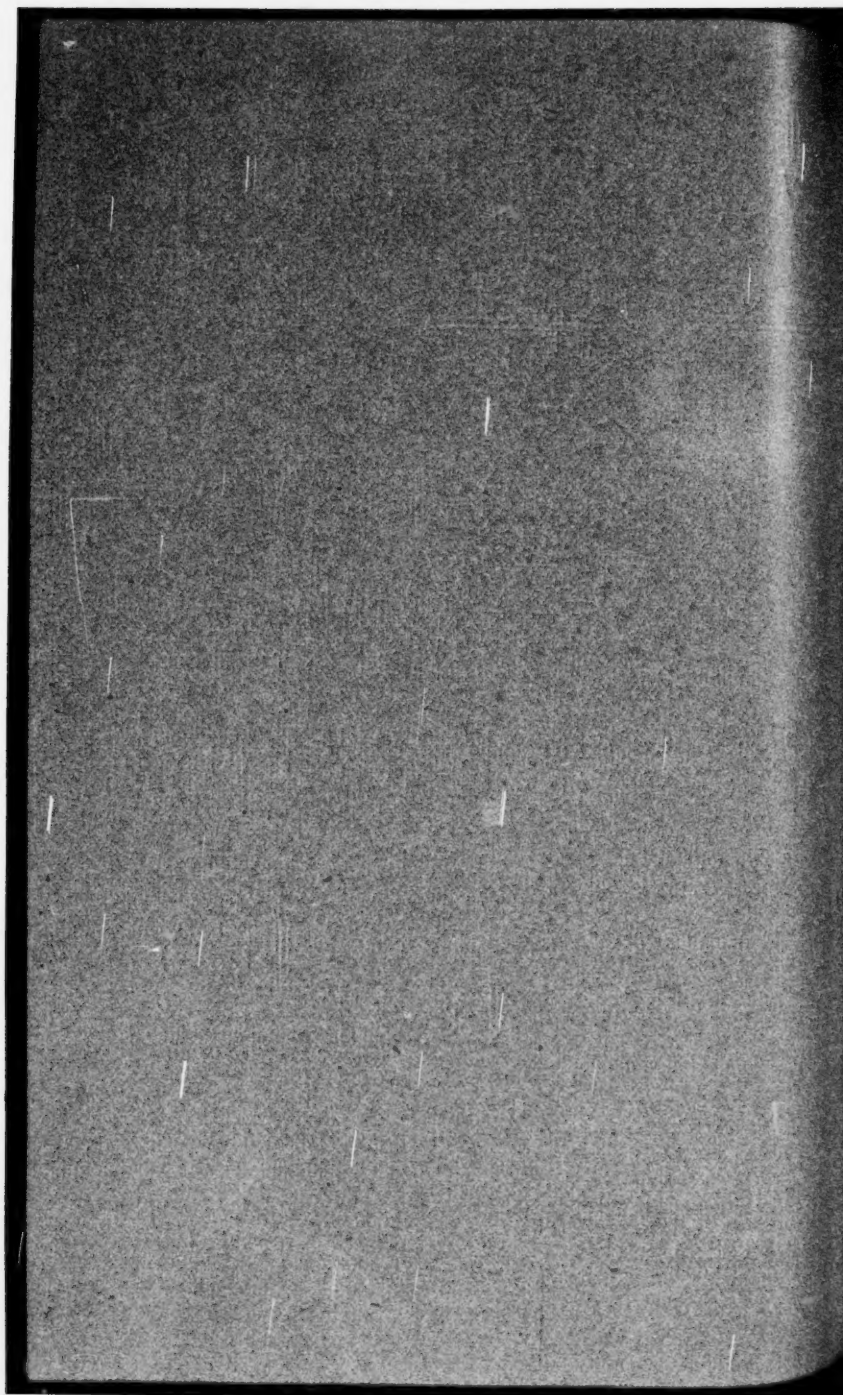
VS.

**FARMERS' LOAN AND TRUST COMPANY, ET AL.,
APPELLEES.**

**BRIEF FOR APPELLEES MORAN BROS. AND
HENRY K. MCHARG.**

(Reprint, omitting immaterial portions.)

L. W. CAMPBELL,
Solicitor for Moran Bros. and Henry K. McHarg, Appellees.



No. 503.

UNITED STATES CIRCUIT COURT OF APPEALS,
FIFTH CIRCUIT.

LACKAWANNA IRON AND COAL COMPANY,
APPELLANT,

vs.

FARMERS' LOAN AND TRUST COMPANY, ET AL.,
APPELLEES.

BRIEF FOR APPELLEES MORAN BROS. AND
HENRY K. MCHARG.

(Reprint, omitting immaterial portions.)

The subject of appellant's intervention is the sale and delivery by the Lackawanna Iron and Coal Company to the Houston and Texas Central Railway Company, prior to the appointment of a receiver over the property of said company, and during the years 1882 and 1883, of 18,581 tons of steel rail at an aggregate cost of \$735,454.30.

The object sought by intervenor in this proceeding is to obtain priority in the payment of its claim over the mortgage bond holders out of the proceeds of the sale of the property, or the net income arising from the operation of the road. The claim was referred to a special master who was ordered to hear evidence and report the facts to the Court. The complainant and these appellees appeared before the master and after pleading the general issue specially pleaded that the claim was stale and barred by laches and barred by the Texas Statute of four years limitation. The master in due time filed his report, which was not excepted to and is copied in full in the record. Upon the hearing a decree was entered dismissing the petition.

First Proposition.

Before a debt contracted by the Railway Company prior to the appointment of a receiver will be given priority over the debt of the bond holders secured by a prior mortgage on the road, it must appear in cases where the debt is for supplies or material, (1) that it is the purchase price of current supplies needed from time to time to keep the road in repair, (2) bought on temporary credit, which credit resulted from the nature and character of railroad business, (3) that such purchase was made within a reasonable time prior to the appointment of a receiver of the property.

STATEMENT.

1. On this subject the master finds: "I find that the debt for which the Lackawanna Company claims payment in its petition, *cannot be classed as a current debt*, made in the ordinary course of business; * * * that the credit

extended under said contracts was at the request of and for the accommodation of the defendant Railway Company, and *upon its general credit, * * ** without any stipulation that security should be given by the defendant company for said rails, or that payment therefor should be made out of any particular fund or in any particular way; that said sale was for *an unusually large amount of rails*, and defendant was unable to pay cash therefor." (R. p. 656.) The magnitude of these dealings become apparent upon an examination of the master's findings. In the period of about fourteen months defendant bought of petitioner 18,581 tons of rail, at an aggregate cost of \$735,454.30, which at 88 and 84.86 tons per mile for 56 and 54-pound rails respectively, were sufficient to reconstruct 214.77 miles of track.

2. The master further finds: "I find that negotiable promissory notes were given petitioner by the defendant company for all rail sold under the three contracts; *that all of said sales were made on a stated credit for a fixed period of time, viz: six months after the average date of each delivery, and that said defendant company had the right, under said contracts, to extend the time six months longer from the maturity of said notes*; that such extensions were made for the accommodation and to suit the convenience of said defendant company and that said extended negotiable notes remaining unpaid matured as shown above in clauses 2 and 3, during the months of February, March, April and May, 1885." (R. pp. 754-5:) The above finding shows that the credit was voluntarily extended, and did not result from the nature of the business or necessities of the case.

3. The sales were not made within a reasonable time

prior to the appointment of a receiver over the property. On this subject the master finds:

"I find that all the rails delivered under the first contract, and about one half of the rails delivered under the second contract were paid for by the Railway Company prior to the appointment of any receiver of said property, but that the remaining half under the second contract, and all rails furnished under the third contract, are not paid for.

"I find that the rails furnished under the *second contract* were furnished under a contract made *a year and ten months prior to* the appointment of the receiver in cause No. 185, and about *three years and three months prior to* the appointment of a receiver in Consolidated Cause No. 198, and about *six years prior to* the appointment of the receiver in *this cause*.

"I find that the rails furnished under the *third contract* were furnished under a contract made about *sixteen months prior to* the receivership in cause No. 185, and about *two years and nine months prior to* the receivership in Consolidated Cause No. 198, and about *five years and six months prior to* the appointment of a receiver in *this cause*." (R. p. 655.)

AUTHORITIES:

1. Must be for indebtedness for current supplies, labor, etc.
- Bound vs. Ry. Co., 58 Fed. Rep., 473.
 Thomas vs. Car Co., 149 U. S., 95.
 Hale vs. Frost, 99 U. S., 389.
 Blair vs. Ry. Co., 22 Fed. Rep., 471.
 Huidkoper vs. Locomotive Works, 99 U. S., 258 and 260.

2. Credit must be temporary and result from the necessities of the business.

Blair vs. Ry. Co., 22 Fed. Rep., 471.

3. Debt must have been contracted short while prior to appointment of receiver.

Thomas vs. Peoria Ry. Co., 36 Fed. Rep., 808.

Turner vs. Indianapolis Ry. Co., 8 Biss. (U. S.) 315.

Fosdick vs. Scholl, 99 U. S., 235.

Union Trust Co., vs. Ill. Mid. Ry. Co., 117 U. S., 434.

Taylor vs. Ry. Co., 7 Fed., 377.

Miltenberger vs. Logansport R. Co., 106 U. S., 286.

Six months seems to be the general rule, which may be deduced from the authorities, and it is only in cases presenting strong equitable features that back debts of longer standing will be given priority. No exceptional equity seems to be claimed in this case, or if claimed none is shown. In this case the last contract was made sixteen months prior to the first receivership and five years and six months prior to appointment of receiver in this cause.

Second Proposition.

The effect and the only effect of a finding that a back debt was contracted an unreasonable time prior to the appointment of a receiver is to take the claim out of the preferred column and place it among the general floating indebtedness of the company, and when this is done by a direct finding that the debt was contracted upon the general credit of the company, it is not material whether it was contracted a reasonable or unreasonable time prior to the appointment of a receiver.

STATEMENT.

The master finds that petitioner's claim is *not a current debt*, and was contracted on the *general credit* of the company. (R. p. 656.)

Thomas vs. Peoria Ry. Co., 36 Fed., 808.

Manchester Locomotive Works vs. Truesdale, 44 Minn., 115.

Third Proposition.

Before such debt will be given priority it must appear that the material was not sold on the general credit of the company.

STATEMENT.

On this subject the master finds as follows: "I find that when the aforesaid contracts were made with the said Lackawana Company both seller and buyer expected the debts to be paid from the net income of the railway; that the credit extended under said contracts was at the request of and for the accommodation of the defendant Railway Company, *and upon its general credit*. That sales were made *without any stipulation that security should be given by the defendant company for said rails, or that payment therefor should be made out of any particular fund, or in any particular way*; that said sales were for an *unusually large amount of rails*; and the defendant was unable to pay cash therefor, and there was no way of obtaining said rails except upon credit; and *petitioner* herein at the time of said contracts and sales *had knowledge of the mortgage of June 16, 1873, given by the defendant Railway Company upon the properties of the Waco and Northwestern division to secure the first*

mortgage bonds, which said mortgage has been herein foreclosed." (R. p. 656.)

The foregoing findings establish that the rails furnished were *upon the general credit of the company*, and that said purchase was for an unusually large amount of rails, and petitioner at the time of said sales had knowledge of the mortgages declared on herein. Such being the case, under no circumstances could petitioner be given priority over the bond holders.

The purchases under the three contracts set up in intervenor's petition are for 20,000 tons and under these contracts in less than fourteen months 18,581 tons were delivered at an aggregate cost of \$735,454.30, being enough rail to lay down a new track outright 214.77 miles. After paying nearly one-half the amount due on these purchases there remains unpaid over \$550,000.00, with interest for six or seven years, making an aggregate amount unpaid on said contracts of about \$850,000.00. From the findings of the master and the facts supporting said findings, it is apparent that this claim belongs to claims known as "claims for material furnished for general and original construction" or for "general merchandise," and where this is the case, the claim under no circumstances is entitled to priority over the mortgage bond holders, either to the proceeds of sale, or net revenue arising from the operation of the road, and it is immaterial under such circumstances whether there has been or not interest paid on the bonded indebtedness, or the erection of permanent improvements on the property.

Thomas vs. Car Co., 149 U. S., 95.

Bound vs. Ry. Co., 58 Fed., 473.

Fourth Proposition.

Before a debt for current supplies will be given priority it must appear that the order appointing the receiver made provision for the payment of such claims and that there has been a wrongful diversion of the current revenues of the road which should or would have been used in the payment of such debt to the payment of bonded interest or permanent improvement of the property covered by the mortgage, and the extent of such priority will be limited to the amount diverted. Neither fact exists in this case.

STATEMENT.

1. There is no provision in any of the orders appointing receivers in causes 185, 198 and 227 for the payment of back debts.

2. There has been no diversion of the income of the road to the payment of bonded indebtedness or permanent improvements which should or would have been used for the payment of petitioner's debt either by the railway company prior to receivership of said property or by any of the receivers since. All interest appears to have been paid on bonded indebtedness up to January 1, 1885, when the first default occurred. No interest has been since paid on first mortgage bonds of the Waco division, except \$91,371.00 paid by order of the Court by the receivers in cause 198 on or about May 1, 1887, being the installments of interest which matured January 1 and July 1, 1885, and interest thereon to date of payment. (R. p. 670.) This is all the interest that has been received by those bond holders for a period of twelve years. The rail in question was sold un-

der two separate contracts; one dated April 26, 1883, under which 5,009 tons of 56-pound rail at \$39.50 per ton were delivered during the months of June, August and September, 1883. (R. p. 651.) The other contract is dated October 30, 1883, under which 8,552 tons of 54-pound rail at \$36.60 were delivered during February, March, April and May, 1884. (R. p. 653.) The contracts of sale provide that the rail is to be paid for in notes at six months with six per cent. interest, with privilege in the Railway Company to extend time of payment six months longer. In accordance with the terms of these contracts, notes were given and which were renewed and extended from time to time, so that all the notes due petitioner matured after January 1, 1885, and during the months of February, March, April and May. (R pp 651 to 653.) Petitioner having extended the time of payment could not in the meantime prior to the maturity of the notes demand payment of said notes, and cannot now complain of interest payments being made before the maturity of its own notes. The record shows that the bonded interest of the railway company was payable semi-annually on January 1 and July 1. Interest was paid January 1, 1883, July 1, 1883, January 1, 1884, and July 1, 1884, by the company. All these payments were long prior to the maturity of petitioner's debt. It can in no sense be said that these interest payments was a diversion of the stream from its natural channel. It cannot be presumed that this would have been paid to petitioner but for the interest payment, for at that time the company owed petitioner no matured debt. Petitioner is therefore estopped by its own contract in first giving time and afterwards extending time of payment from claiming the money used in paying interest on the bonded debts from the date of the sale in 1883 to

maturity of its debts in February, March, April and May, 1885.

Our position is that petitioner cannot complain of the payment of any valid debt of the company which was in existence when the rail was sold, and of which it had notice, and which matured prior to the maturity of petitioner's debt. This would give all interest installments which matured prior to February, March, April and May, 1885, priority over the debt of petitioner, and of course would include the installment of interest which matured January 1, 1885.

The receivers in cause 185 were appointed February 20, 1885, and the property has been in the possession of receivers in causes 185, 198 and 227 continuously since. As stated above no interest was paid in causes 185 or 227, and of the payments made May 1, 1887, one-half was for interest which matured January 1, 1885, and which matured prior to the maturity of any of petitioner's notes, and which petitioner must have understood would be paid at maturity. The whole of said interest payment of May 1, 1887, was made on application to the Court in cause 198, to which cause petitioner was a party. If petitioner was in law or in fact entitled to said fund in preference to the bond holders, in that cause, and on that occasion, was the time and place to have asserted its right thereto. Besides the order was made without prejudice. On this subject the master finds:

"I find that said order expressly declared that it was 'without predjudice to the rights of defendant or of any intervenor in this cause, or any final decree to be rendered in the same, nothing herein being decided as to the merits of the claim of the defendants, or of intervenors, and this or-

der not in any manner stopping or affecting the rights of any party or intervenor in this cause.'” (R. p. 674.)

If this money was received by the bond holders without prejudice they are surely not to be harrassed in after years in a separate suit with a serious charge that this interest was wrongfully taken from one of the very creditors who was a party to the cause and participated in taking the order. The bonds and mortgage securing same are admitted to be valid and unpaid, and if the bond holder is not protected by the above provision against the charge of diversion in accepting this interest, then it may be truly said that this money was taken with great probability that the act of doing so would be very prejudicial, indeed, to the extent of refunding every dollar received with interest thereon at the end of an expensive lawsuit. The order was doubtless intended to provide for the payment of a debt which was conceded to be valid, but that in doing so no precedent should be established as to who was entitled to priority in payment out of the net income or proceeds of sale of the road as a protection to petitioner and other parties and intervenors who were asserting priority over the bond holders, and that the bondholder, on the other hand, in accepting the money, should not be charged with diverting that money from the other claimings.

If the above is a valid interpretation of the order it is manifest that no diversion has been shown by way of interest payment. It only remains to be considered whether there has been a wrongful diversion of funds in the erection of betterments and permanent improvements on the Waco branch. On this subject the master finds:

“I find that no interest has been paid on the bonded in-

debtedness by either of the receivers in this cause; I find that Alfred Abeel, receiver in this cause, has expended, under the orders of this court, \$46,505.40, for betterments and permanent improvements, from December 10, 1892, to September 3, 1895, consisting of bridges, shops and round-houses, car shed, water stations, locomotives, chair car and fencing." (R. p. 663.)

"I find that no part of the income arising from the operation of the road and no part of the proceeds of sales of old rails, old iron, old cars and engines, which was received by the receivers in causes Nos. 185 and 198, ever came into the possession of the receiver in this cause, and the evidence fails to show that any part of the new equipment purchased by the receivers in causes Nos. 185 and 198, as shown above, ever came into the possession of the receivers in this cause. The evidence fails to show that any improvements and betterments of the property added to the property of the Houston and Texas Central Railway Company by the receivers in causes Nos. 185 and 198, were made on the Waco and Northwestern division." (R. p. 664.)

"I find that prior to April 6, 1889, no separate accounts were kept of the receipts and disbursements of the Waco and Northwestern division, but the same was operated as a branch of the general system of the Houston and Texas Central Railway Company, and the evidence fails to show what, if any, of the expenditures made by the receivers in causes Nos. 185 and 198 for extraordinary repairs, betterments and improvements and for operating and running expenses were made for said Waco and Northwestern division, and what portion for the other division of said Houston and Texas Central Railway Company; and this is true also as to receipts and incomes." (R. p. 664.)

"I find that the receivers in cause No. 185, had on hand in cash at the opening of business on January 21, 1886, \$175,393 65, but there is no evidence that any part of said fund came into possession of the receivers in this cause." (R. p. 664.)

"I find that the receiver in cause No. 198, had on hand at beginning of business on April 6, 1889, cash amounting to \$215,842.45, but the evidence does not show that any part of said funds came into the hands of the receivers in this cause." (R. p. 664.)

The above findings show that the only betterments added to the Waco branch in the long period of time covering over eleven years, was \$46,505.40 for betterments and permanent improvements from December 10, 1892, to September 3, 1893, consisting of bridges, shops, and round-houses and car sheds, water stations, locomotives, chair car and fencing. The first expenditures for these betterments (December 10, 1892) were made nearly eight years after maturity of petitioner's notes and the last (September, 1895,) were made over ten and a half years thereafter. At this time, unless suit had been instituted on the notes they would have been long since barred by limitation, and it could not be held that this fund arising from the operation of the road a decade after the rail were furnished was the current revenue which should have been applied to the payment of petitioner's debt. If this were so there would be no current fund available for the payment of current expenses and the necessary improvements from time to time required to keep the road "a going concern." No Court has ever held that expenditures, so far removed by time, place and circumstance from the claimed current indebtedness to

amount to a diversion. But, aside from this, these expenditures were all made under the orders of this Court, in this cause, to which petitioner has been a party since 1891. The right to order such expenditures and the necessity therefor has been long since determined by this Court, and such orders estop and conclude petitioner.

Bound vs. Ry. Co., 58 Fed., 473.

Central Trust Co. vs. Chattanooga Ry. Co., 69 Fed., 295.

Cutting vs. Ry. Co.; 61 Fed., 150.

The foregoing argument is based on the assumption that it was found by the master that the interest payment of \$91,371.00, in May, 1887, on the Waco & Northwestern division bonds, was made *out of the current revenues of the road*. On this subject the master finds that the accounts were not kept in such a manner as to indicate the exact fund out of which the interest payments were made, and that no separate account was kept of the earnings of the Waco & Northwestern division as distinguished from the earnings of the other division. And he nowhere finds that this interest was paid out of the income. (See his findings R. pp. 664, 670 and 680.) The same is true as to the expenditures for betterments and new equipment. The master finds that the only expenditures made for that purpose on the Waco & Northwestern division was made by receiver Abeel after December 10, 1892, and prior to September 3, 1895, and amounted to \$46,505.40. (R. pp. 663-4.) But there is no finding that these expenditures were made *out of the current income*. The finding is simply that this amount of money was used for that purpose. The burden was on appellant to prove that the expenditures, which it is claimed amounted to a diversion of the current income, were, in

fact, made from *that* fund. The findings leave appellant's case without equitable support. For the only real equity relied on by appellant to establish the claimed priority, was the alleged diversion of current income from the payment of supply creditors to the payment of interest on the bonded indebtedness and the erection of permanent improvements upon the mortgaged property.

Appellant would not be entitled to recover on the ground that it furnished the rail that went into the road, because this rail was sold on the "general credit of the company," was no part of the "current supplies," was part of an "unusually large purchase" without any understanding that the rail "should be paid for in any particular way or out of any particular fund." Besides, the findings show that the rail was furnished twelve to thirteen years ago, and there is nothing in the record to show to what extent, if any, the rail enhanced the value of the mortgage security, or that the road has earned a greater net revenue or sold for a greater price as a result of the placing of this rail in the road. There are no findings whatever on these issues. Appellant is in no position to complain of the sudden action of the court in appointing receivers in cause 185 in February, 1885, for in a short while thereafter appellant intervened in said suit, joined the Southern Development Company in its prayer for a receiver, and in all things ratified the acts of that company. R. p. 661.

Cutting vs. R'y Co., 61 Fed., 150.

Central Trust Co. vs. R'y Co., 69 Fed., 295.

Case of Bound vs. Ry. Co., 58th Fed., 473, is in point. In that case this same company, the Lackawanna Iron and Coal Company, intervened on precisely the same character of

claim as asserted here for the price of steel rails sold to the Railroad Company on a credit of eight months, and the sale was made eighteen months prior to the appointment of the receiver, and said rails were necessary to the maintenance of the road, and were sold on the promise of the president of the road that they were to be paid for out of the earnings, but this promise was not fulfilled. The notes were extended from time to time, and during the interval before the maturity of the first note \$33,000.00 was paid on account of interest due the mortgage bond holders. It was claimed by intervenor there, as is claimed here, that because its debt was for material which went into the road, improving its condition, and because there had been a diversion of the current debt fund to the payment of interest on mortgage bonds, it was entitled to displace the bond holders to the extent of such interest payment. The claimant prevailed in the lower Court, and the displaced bond holders appealed to the Circuit Court of Appeals. Chief Justice Fuller, acting as Circuit Justice, and Judges Hughes and Morris composed the Court, and in passing on and deciding the claim of intervenor there asserted, the Court say: "The rule giving preference to current expenses incurred on the faith of the earnings of a railroad shortly before the appointment of a receiver has never been carried so far. The debt of the Lackawana Company was an ordinary merchandise debt. The road being heavily mortgaged all that any unsecured creditor had to look to was the earnings. The immediate earnings, it is clear, the Lackawana Company did not look to, as the sale was on a credit of eight months. It must be inferred, therefore, that it was expected that interest on the mortgage debts was meanwhile to be paid during the running of the credit, otherwise a foreclosure would have been

imminent within three months after the sale of steel rails was made. The claim is quite different from those ordinary and necessary expenses of operating a railroad contracted but a short time before a receivership, and which by the sudden action of a Court in appointing a receiver, are left unpaid."

Fifth Proposition.

Though it may appear that petitioner's claim on some of the grounds asserted in whole or in part, is entitled to an equitable priority over the mortgage bond holders, such priority will not be decreed in this case, but petitioner will be remitted to its intervention in cause No. 198, because (1) it would be inequitable and unjust to charge the proceeds arising from the sale of road—made more than eleven years after the purchase of said supplies—and the net revenues arising from its operation from five to eleven years thereafter, with payment of such debt, and (2) it appears that the receivers in causes Nos. 185 and 198, from February 20, 1885, to April 6, 1889, a period of over four years, immediately after petitioner's debt matured, operated the whole H. & T. C. system, including the Waco branch, took all its revenues and profits during these four years, took 2,960 tons of old iron rail from the Waco branch and disposed of same at a net price of \$13 00 per ton, aggregating \$38,480.00, used the proceeds from the sale of this rail and the revenue of this branch for the purchase of new cars, locomotives and other equipments and the erection of betterments and permanent improvements of the main line and Austin branch, and (3) it appears that this branch during these four years received no betterments or permanent improvements, and the receivers in this cause re-

ceived no part of the new cars, locomotives and other new equipments purchased by the receivers in causes 185 and 198 and have never come into the possession of any of the revenues arising from the operation of said road during the years 1885 to 1889 or the proceeds from the sale of said old iron rail, and because the bond holders secured by the mortgage declared on herein asked no equitable relief in said causes, 185 and 198, and received no part of the proceeds of the sale of the road in said causes.

STATEMENT.

On the subject here discussed, see master's finding No. 16. (R. pp. 663 4.)

On the subject of receipts and expenditures of the entire system by the receivers in causes Nos. 185 and 198, the master finds as follows :

"I find that during the receivership of Clarke & Dillingham, in said cause No. 185, they received from the operation of the Railway company, revenues, and expended for operating expenses, taxes, etc., the following amounts, to-wit:

Amount received from Febuary 23, 1885, to January 21, 1886, two million, seven hundred and fifty-eight thousand, four hundred and eighty-seven and 40-100 dollars	2,758,487.40
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Operating expenses, taxes, etc., same period ..	2,137,322.44
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Balance or surplus	621,164.96
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Amount received from January 21 to July 10, 1886, one million, one hundred and forty-three thousand, seven hundred and thirty-one and 05-100 dollars	1,143,731.05
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For operating expenses, etc., for the same period..... 1,341,753.85

Leaving a deficit for this period of.....\$198,022.80

And leaving a net balance from the operation of said railways from February 23, 1885, to

July 19, 1886, of.....\$423,142.16

XIX.

"I find that when said Clarke & Dillingham took possession of the property of the defendant railway company on February 23, 1885, they received in cash \$30,416.34.

That they collected assets of the company as follows, to-wit:

Traffic balances and other claims.....	118,730.08
Sales of old rails on hand February 23, 1885	110,275.00
Sale of old cars	6,500.00

Total.. \$265,921.42

Amount expended in paying liabilities of the defendant Railway Company \$23,274.20

Interest paid upon the first mortgage bonds of the company, being interest due January 1, 1885, to July 1, 1885..... 751,438.15

Amount expended for new steel rails..... \$245,793.64

Amount expended in payment of certain car.. trust notes..... 125,695.44

Amount expended for new passenger coaches, baggage, mail and express cars, etc., and locomotives..... 265,696.33

Amount expended by said receivers for right of way, fencing, track, real estate, depot, roundhouse, foundry and pattern house at Houston.....	126,218.62
Total.....	\$1,536,116.38

"I find that the amount expended as above, \$384,026.20, was expended under the receivership of Messrs. Clarke & Dillingham."

"The above statement shows receipts and expenditures to January 9, 1888, the date when Master Winter, heard the evidence on this intervention in cause No. 198, but no proof has been offered before me, showing the receipts and disbursements of the receivership in said consolidated cause since said hearing before said master on January 9, 1888."

XXI.

"I find that said Easton and Rintoul and Dillingham during their receivership realized out of proceeds of sale, or collection of old assets of the defendant company, the sum of \$135,889.70."

XXII.

"I find that the receivers in cause No. 198 received from the receivers in cause No. 185, the sum of \$138,751.37 in cash."

"I find that the receivers in consolidated cause No. 198, after they took possession of the assets of the Railway Company on July 10, 1886, and up to the time of the filing

of the report of master, Winter, paid liabilities of the receivers, Clarke & Dillingham, taxes, outstanding vouchers, pay rolls, traffic balances, \$221,421.32, and collected from the amount due said Clarke & Dillingham as receivers in cause No. 185, \$39,016.69."

The above statement shows that the receivers in cause No. 185 expended for betterments as follows:

Amount expended for new steel rails.....	\$245,793.64
Amount expended in payment of certain car trust notes	135,695.44
Amount expended for new passenger coaches, baggage, mail and express cars and locomotives	265,693.33
Amount expended for right of way, fencing track, real estate, depot, roundhouse, foundry and pattern house at Houston....	126,218.03
Making a total of.....	<u>\$763,404.63</u>

This entire amount, \$763,404.03, was expended in making betterments and improvements, and the purchase of new equipments, etc., on the main line and Austin branch, and no benefit thereof has ever accrued to the Waco branch. The above amount was undoubtedly paid out of the current revenue of the road, and the Waco branch was entitled to its proportionate share. The findings show that no separate account was kept and in the absence thereof, the only equitable division would be on a mileage basis. The Waco branch is about one-ninth in length of the mileage of the entire system and would be equitably entitled to receive out

of the above fund \$84,822.67 in betterments and permanent improvements when in fact it received none. In addition to the above statement the findings show that the receivers in cause No. 185 sold 2960 tons of old rail taken from the Waco branch, on which these bond holders had their mortgage, at \$13.00 per ton, making an aggregate of \$38,480.00. The findings show that no part of this fund has ever come into the hands of the receivers in this cause. This amount added to the above sum of \$84,822.67 makes a total of \$123,302 67, that has been wrongfully (as against these bond holders) taken from the Waco branch, and used in the erection of improvements upon the main line and Austin branch. The findings show that 6.2 miles of the Waco branch was laid with rails furnished under the first and second contracts, but no proof was introduced showing what proportion was furnished under each. The findings show that all rails furnished under the first and about one half furnished under the second contract were paid for by the Railway Company prior to any receivership over the property. Such being the findings, no amount has been shown to be unpaid to petitioner for the 6.2 miles. The findings show further that 30.8 miles of the Waco branch was laid with rails furnished under the third contract, being the 54-pound rail, and that it requires 84.86 tons of said rail to lay a mile of track, which makes 2,613.68 tons of rails on the 30.8 miles. The purchase price of this rail is \$36.60 per ton, making a total of \$94,560 68, the original cost price of the total rail unpaid for on the Waco branch. Deducting this amount from the \$123,302 67 leaves an excess of \$28,741 99 that has been wrongfully taken from the Waco branch and appropriated and used on the main line and Austin branch for permanent improvements and betterments, after fully pay-

ing for all steel rails unpaid for on the Waco branch. These figures show that a great wrong has already been committed to the extent of over \$28,000.00 and if the fund now in Court should be used in the payment of the 30.8 miles of steel rail another and a greater wrong by far would be committed, but should the receivers in cause No. 198 be required to pay for these rails justice to that extent would be attained.

The foregoing makes it apparent that the petitioner should be remitted to its intervention now pending and undetermined in said cause No. 198. The lower Court still has jurisdiction over both causes, and entire control of these interventions.

These views were urged upon the attention of the trial Court and it may be that they had the desired influence in the termination of the case. There is no assignment of error covering this feature of the case.

Sixth Proposition.

Petitioner alleges as one of its grounds of priority that there is a provision in the mortgage declared on herein, allowing the trustee, in case it takes possession of the property under the terms of the mortgage, to pay the floating indebtedness of the company, and that it relied on said provision in selling the rails to the defendant Railway Company. But there is, in fact, no such provision in the mortgage.

STATEMENT.

On this subject the master finds as follows:

"I find in the mortgage given by the Houston and Texas

Central Railway Company to the Farmers' Loan and Trust Company, trustee, dated June 16, 1873, being the same mortgage declared on herein, the following provisions:

“And in case the said Houston and Texas Central Railway Company shall fail to pay the principal, or any part thereof, or any installment of the interest, or any part thereof, on any of said bonds at any time when the same shall become due and payable according to the tenor thereof and for sixty days after having been demanded, it shall be competent for the said trustee, its successors or assigns, to enter upon the said railway and premises and property herein conveyed, by its attorneys and agents, and take possession of same without let or hindrance of the said first party and every part and parcel thereof, and the appurtenances, and appoint an agent to operate and manage the same, and receive the revenue and income thereof, applying the said funds, after deducting taxes, necessary expenses and counsel fees, to keep the same in good order and repair, and the surplus to pay the principal and interest of all the bonds which may be due and outstanding, and secured hereby, pro rata, and thereafter, to the payment of any contributions due to the sinking fund herein established. And upon the request of the holders of one-fifth in amount of the bonds so in default which may be at any time outstanding under this deed of trust, it shall be the duty of said second party by its president, or agent duly appointed in its behalf, to enter upon and take actual possession, with or without entry, or foreclosure of said railway and property herein described, and all and singular each and every part and parcel thereof, and assume its management until the arrears of both principal and interest be paid, or the prop-

erty sold, as herein drescribed, receiving the rents, revenue and income thereof and applying them in the same manner as above stated.

“It is, however, expressly agreed that the said party of the first part may dispose of the current net revenues and income of all the said property and railway hereby conveyed in such a manner as it shall deem best, until default shall be made in the payment of the interest or principal of said bonds, or of any one or more of them, and shall have the right to sell and dispose of any of such real estate or other property as it may own or acquire, which may not be needed or acquired for the purposes and business of the said Waco and Northwestern division, except in the case of the six thousand acres per mile of completed road, and which sale and conveyance of such outside property shall transfer the said property and title free from encumbrance of this mortgage or deed of trust, and to change its tracks and make any and all alterations necessary for the benefit of the same.’

“I find that there is no provision in said mortgage, that the trustee may, if it acquires possession of said railway under said mortgage, pay any floating debt, or debts, of said company out of the gross earnings of said railway.” (R. pp. 664 to 666.)

This suit was filed by the trustees for the mortgage bond holders in the mortgage declared on herein on April 6, 1889, and at the suit of said trustee this Court placed the railroad and other property covered by the mortgage in the hands of a receiver, complainant's bill setting up the above provision contained in the mortgage declared on, claiming a lien on the corpus of the property, and the earnings of the

road after the same was placed in the hands of the receiver. Petitioner did not intervene in this cause until more than two years after, and on to-wit: November 3, 1891, simply setting up its priority, and nothing more.

AUTHORITIES.

Dow vs. Memphis & Little Rock R. Co., 124 U. S., p. 652.

(S. C.) 33 Am. & Eng. R. R. Cases, p. 12.

Sage vs. Memphis & Little Rock R. Co., 125 U. S., 361.

(S. C.) 35 Am. & Eng. R. R. Cases, p. 40 and cases therein cited.

Argument.

The merits of appellant's claim for priority is made to rest solely upon the supposed existence of this clause in the mortgage. (R. p. 627.) From this allegation it plainly appears that appellant when selling these rail and in extending the time, it was fully recognized that no superior equity existed over the mortgage, or if any existed it was not relied on. Instead of selling these rail upon the belief that priority would be given upon principles of equity, appellant seems to have made the sales with full knowledge of the existence of the mortgage, and with the understanding that a contract had already been made for its benefit and perfect protection, in that the mortgage contained a clause which required appellant's debt to be paid in any event. This allegation not only shows upon what security appellant relied, but it shows, with equal clearness, the *rank* and *character* of appellant's claim. It shows that appellant, in selling the rail and in placing reliance upon this clause understood its claim to be a mere "floating debt," for the supposed clause relied on provides, according to the allegation, for the pay-

ment of "floating debts" only. But this particular mortgage contained no such provision. The foundation having failed the superstructure cannot stand. The evidence shows that a number of mortgages given by defendant company were in existence at this time. It is probable that one or all the others contained some such stipulation. Be this as it may, by the allegation above we are given appellant's own version of the rank of its claim, and the security upon which the rail was sold. Having relied on that security no other can now be claimed in the present condition of the record. "The express mention of one thing implies the exclusion of another," is a legal maxim which controls the language of this pleading. We concede that this is not a rule amounting to estoppel. The petition could have been amended and a different set of facts alleged, and if true, been proven. But nothing of the kind has occurred. No amendment, no change. The case went before the master and trial court and is brought here claiming and asserting, in the strongest language, that the mortgages contain this clause and that appellant relied on the contract therein made for its benefit in selling the rail, has in all things accepted its terms and conditions, and bases its suit thereon. The allegation makes a case of a lien created by express contract for the benefit of "floating debts," with an unqualified acceptance by appellant. If he relied on this supposed express contract he did not rely on the equity asserted by the assignments of error. But the master finds "that both seller and buyer expected the debts to be paid from the *net* income of the railway." (R p. 656) This understanding that the claim was to be paid from the *net* income, as distinguished from the current or gross income, effectually took this claim out of the preferred column and placed it among the general floating indebted-

ness of the company. This, in connection with the further finding of the master, that the rail was sold on "the general credit of the company," that it "was not a current debt," and that the "purchase was of an unusually large amount of rail," "without any stipulation that security should be given by the defendant company, or that payment therefor should be made out of any particular fund or in any particular way," taken in connection with the above allegation, that the rail was sold relying upon the supposed terms of the mortgage, rendered the trial court powerless to prefer appellant's claim.

20 Am. & Eng. Ency. of Law, p. 431, note 3.

Broom's Legal Maxim, p. 650.

Wood vs. Guaranty Co., 128 U. S., 416.

Adison vs. Lewis, 9 Am. & Eng. Ry. cases, 702.

Seventh Proposition.

The master finds substantially that when the contracts were entered into the condition of the track of the railway company was such that the demand for new rails upon the most worn portions was practically imperative; that for a number of years prior to December, 1882, only about 5,000 tons of new rails had been purchased; that the condition of the road was bad, except such portions as had been relaid with said 5,000 tons; that there was continuous breakage of rails, and wrecking of trains; that the track was unsafe, and was generally so regarded, not only by railroad men, but by the traveling public; that the damage to merchandise, rolling stock, etc., was continuous, and the need of new rails appears to have been absolutely necessary as a preservation of human life, the loss of which was liable to occur at any time; that when the contracts were made both seller and buyer expected the debt to paid from the net income of the road;

that the credit extended under said contracts was at the request of, and for the accommodation of the Railway Company, but he finds further that the rails were sold upon the general credit of the Railway Company, and that said sales were made without any stipulation that security should be given by the defendant company for said rails, or that payment therefor should be made out of any particular fund, or in any particular way; that said sales were for an unusually large amount of rails, and the defendant company was unable to pay cash therefor, and that petitioner at the time of said contracts and sales had knowledge of the mortgage declared on herein.

The findings further show that the bonded indebtedness of the Railway Company, when the rails were sold, was \$16,874,500, which was \$33,087.20 per mile, and the floating indebtedness in 1884 was \$3,584,251.30. That petitioner knew of the bonded indebtedness of the company, and probably knew of its floating indebtedness, both of which were large, and hoped and expected to realize the amount of the sales out of the net income of the road, but for no other reason, as no promise was made to that effect.

We submit that the foregoing findings show that the Railway Company had operated its road until its track had become practically worn out, and that it had become suddenly necessary to rebuild anew its entire track. It was, therefore, necessary to purchase an unusually large amount of rails. For this reason the rails were sold upon the general credit of the company, upon long time of payment, and the purchases cannot be classed as other than material bought for general and original construction.

STATEMENT.

The master finds: "I find that the debt for which the Lackawanna Company claims payment in its petition herein cannot be classed as a current debt made in the ordinary course of business as those terms seem generally to be understood, yet it appears that at the time when the contracts hereinbefore mentioned were entered into between said Lackawanna Company and the defendant Railway Company that the condition of the track of the defendant Railway Company was such that the demand for new rails upon the most worn portion of the roadway was practically imperative. For a number of years prior to December, 1882, only about 5,000 tons of new rails had been purchased. The road north from Houston for 90 miles was built in 1857, 1861, and thence northward to Denison, 1867, 1872. The western division leading to Austin was constructed in part prior to 1861, and completed in 1873, and the Waco division was completed about 1875. The condition of these roads was bad, except such portions as had been relaid with 5,000 tons of rails purchased prior to December 28, 1882. There was continual breakage of rails and wrecking of trains, the track was unsafe, and was generally so regarded, not only by 'rail-road men,' but by the traveling public; the damage to merchandise, rolling stock, etc., was continuous and the need for new rails appears to have been 'absolutely necessary as a preservation of human life; the loss of which was liable to occur at any moment.'

"I find that when the aforesaid contracts were made with the said Lackawanna Company both seller and buyer expected the debts to be paid from the net income of the railway; that the credit extended under said contracts was at the

request of and for the accommodation of the defendant Railway Company, and upon its general credit; that said sales were made without any stipulation that security should be given by the defendant company for said rails, or that payment therefor should be made out of any particular fund or in any particular way; that said sales were for an unusually large amount of rails, and the defendant was unable to pay cash therefor, and there was no other way of obtaining said rails except upon credit; and petitioner herein at the time of said contracts and sales had knowledge of the mortgage of June 16, 1873, given by the defendant Railway Company upon the properties of its Waco and Northwestern division to secure the first mortgage bonds, which said mortgage has been herein foreclosed."

"I find that the steel rails supplied by said Lackawanna Company, under the aforementioned contracts, 18,581 tons, were placed in the track of the defendant Railway Company as soon as received."

VII.

"I find that the bonded debt of the defendant Railway Company January 1, 1885, was as follows:

1st mortgage, main line, 7 per cent	\$6,262,000
1st mortgage, Western division, 7 per cent....	2,270,000
1st mortgage, W. & N. W. Div., 7 per cent....	1,140,000
Consolidated M. L. & West. Div., 8 per cent...	4,118,000
Consolidated W. & N. W. Div., 8 per cent....	84,000
General mortgage, 6 per cent.....	3,000,000
Income and indemnity.....	500

Total.....\$16,874,500

If the foregoing findings do not show the claim of the petitioner to be in every sense in which those terms are used, "a claim for general and original construction," it is more analogous to that class than to any other class of claims usually asserted in this character of litigation, and we believe that the authorities governing that class of claims should be applied to petitioner's claim."

AUTHORITIES.

Wood vs. Guaranty Co, 128 U. S., 416.

Addison vs. Lewis, 9 Am. & Eng. R. R. Cases, 702.

Am. L. & T. Co. vs. East, etc., Ry. Co., 46 Fed. Rep., 101.

Eighth Proposition.

A claim will not be decreed priority because the material furnished was necessary to the maintenance of the road and to keep it a going concern, for if this were so a party who loaned the Railway Company money in time of financial distress would occupy a position superior to all others and be entitled to the greatest consideration, for money is representative of all material wants, and will serve every purpose toward the maintenance of the road and keep it a going concern.

Morgan's L. & T. Ry. Co. vs. Texas Central Ry. Co., 137 U. S., 171.

(S. C.) 45 Am. & Eng. Ry. Cases, 631.

Tenth Proposition.

Appellant would not be entitled to priority by virtue of the laws of Texas as claimed, because the only law of that

state that pretended to give the claimed priority has long since been declared by the Supreme Court of Texas to be unconstitutional.

Giles vs. Stanton, 86 Texas, 620.

Receivers vs. DuBose, 87 Texas, 78.

In conclusion, we beg to quote from a few of the leading cases on the subjects discussed in this brief. In the case of Blair vs. Ry. Co., 22 Fed. Rep. 474, Mr. Justice Brewer has drawn a clear distinction between sales of supplies made on time voluntarily extended to the road and those made on temporary credit resulting from the peculiar nature of railroad business, affirming that business of such magnitude cannot be transacted on a cash basis, and that in the very nature of this business, *temporary credit* is indispensable. He says:

"The idea which underlies them, I take to be this: That the management of a large business, like a railroad business, cannot be conducted on a cash basis. Temporary credit in the very nature of things is indispensable. Its employes cannot be paid every month. It cannot settle with other roads its traffic balances at the close of every day. Time to adjust and settle these various matters is indispensable. Because in the nature of things this is so, temporary credit must be taken as assented to by the mortgagees, because both the mortgagees and the public are interested in keeping up the road, and having it preserved as a going concern, and whatever is necessary to accomplish this result must be taken as assented to by the mortgagees."

In Heidekoper vs. Locomotive Works, 99 U. S., 260, it is said by Chief Justice Waite: "The Railroad Company

contracted to buy the engines and pay a certain price. The locomotive company retained a paramount lien to secure the sum to be paid. The debt so incurred was not paid * * * So far as we can see no equitable claim upon any fund in Court has been established as security for this debt. The locomotive company occupies the position of a general creditor with no special equities in its favor."

The amount claimed in the above case was a balance due after the lien on the locomotive had been foreclosed.

In the case of *Kageland vs. Am. Loan Co.*, 136 U. S., 97 and 98, Mr. Justice Brewer used this very forcible language in reference to the character of claims here asserted: "Upon these facts, we remark, first, the appointment of a receiver vests in the Court no absolute control over the property, and no general authority to displace vested contract liens. Because in a few specified and limited cases this court has declared that unsecured claims were entitled to priority over mortgage debts, an idea seems to have obtained that a Court appointing a receiver acquires power to give such preference to any general and unsecured claims. It has been assumed that a Court appointing a receiver could rightfully burden the mortgaged property for the payment of an unsecured indebtedness. Indeed, we are advised that some Courts have made the appointment of a receiver conditional upon the payment of all unsecured indebtedness in preference to the mortgage liens sought to be enforced. Can anything be conceived which more thoroughly destroys the sacredness of contract obligations? One holding a mortgage debt upon a railroad has the same right to demand and expect of the Court respect for his vested and contracted priority as the holders of a mortgage lien on a farm or lot. So,

when a Court appoints a receiver of railroad property, it has no right to make that receivership conditional on the payment of other than those few unsecured claims which, by the ruling of this Court, have been declared to have an equitable priority. No one is bound to sell to a railroad company, or to work for it, and whoever has dealings with a company whose property is mortgaged must be assumed to have dealt with it on the faith of its personal responsibility, and not in the expectation of subsequently displacing the priority of the mortgage liens. It is the exception, and not the rule, that such priority liens can be displaced. We emphasize this fact of the sacredness of contract liens, for the reason that there seems to be growing an idea that the chancellor in the exercise of his equitable powers, has unlimited discretion in this matter of the displacement of vested liens. *Railroad Co. vs. Railroad Co.*, 125 U. S., 658, 673. So that these intervenors acquire no right of priority by virtue of their antecedent contracts of sale."

To the authorities cited in this brief, we add the following:

1. On the question of allowing back debts of longer standing than six months:

20 Am. & Eng. Ency. of Law, p. 425 and cases cited.

Blair vs. Ry. Co., 22 Fed. Rep., p. 471.

In re Kelly, 5 Fed. Rep., p. 846.

2. On the question of the propriety of a Court of equity to give claims of the character herein asserted priority over a prior mortgage:

Forman vs. Central Trust Co., 71 Fed. Rep., p. 776.

Railway Company vs. Cowdy, 11 Wall, 482.

Central Trust Co. vs. Chattanooga Ry. Co., 69 Fed. Rep., 295.

- Thompson vs. Valley Ry. Co., 132 U. S., 68.
 Farmers' & Merchants' Nat. Bk. vs. Ry. Co., 36 S. W. R., 131.
 Foggs vs. Blair, 133 U. S., 534.
 Toledo Ry. Co. vs. Hamilton, 134 U. S., 296.
 Trustees vs. Ry. Co., 2 Wood, 542.
 Denison vs. Ry. Co., 4 Biss, 416.
 High on Receivers, Sec. 394a.
 Express Co. vs. Ry. Co., 99 U. S., 191.
 Turner vs. Ry. Co., 8 Biss, 315.
 Miltenberger vs. Ry. Co., 106 U. S., 286.
 Trust Co. vs. Souter, 107 U. S., 591.
 Burnham vs. Bowen, 111 U. S., 776.
 Blair vs. Ry. Co., 22 Fed. Rep., 471.
 L. C. & N. Co. vs. Ry. Co., 29 N. J. Eq., 252.
 Hale vs. Frost, 99 U. S., 389.
 In re Kelly, 5 Fed. Rep., 846.
 Bridge Co. vs. Douglas, 12 Bush, 673.

We submit, with confidence, that appellant has not shown that it is entitled to equitable priority of payment, either out of the proceeds of sale or net income arising from the operation of the road, or that there is error in the decree appealed from and we request that it be in all things affirmed.

L. W. CAMPBELL,

Solicitor for Moran Bros. and Henry K. McHarg, Appellees.

451. Moran Bros.
and Opp. to Board of Directors
for the President
Filed Dec. 11, 1897.

UNITED STATES CIRCUIT COURT OF APPEALS

FIFTH CIRCUIT

No. 508

LACKAWANNA IRON & COAL COMPANY,
APPELLANT,

VS.

FARMERS' LOAN AND TRUST COMPANY ET AL.,
APPELLEES.

SUPPLEMENTAL BRIEF OF MORAN BROS. AND HENRY K.
McHARG.

(REPRINT.)

L. W. CAMPBELL,

Solicitor for Appellees Moran Bros. and Henry K. McHarg.

UNITED STATES CIRCUIT COURT OF APPEALS.

FIFTH CIRCUIT.

No. 503.

LACKAWANNA IRON & COAL COMPANY,

APPELLANT,

versus

FARMES' LOAN AND TRUST COMPANY ET AL.,

APPELLEES.

SUPPLEMENTAL BRIEF OF MORAN BROS. AND HENRY K.

McHARG.

(REPRINT.)

A supplemental brief is made necessary, because the brief filed within the time prescribed by the rules for appellees was prepared without any opportunity to see the brief for appellant, and was prepared upon the supposition that appellant's brief, when prepared and filed, would be predicated upon appellant's assignment of error, and in accordance with the rules of this court. Because this has not been done, and because of many inaccuracies, omissions, misstatements of the record, and violations of the rules of this court in the

preparation of said brief, we file this our supplemental brief and argument.

First.—We find in appellant's brief, from pages 1 to 5, a statement of what purports to be the substance of appellant's petition. Our principal objection to this is that it omits to state the very material allegation that appellant in selling the rail relied for its security upon the supposed existence of a clause in the mortgage declared on herein providing for the payment of floating debts in case of default, and possession is taken under the terms of the mortgage (see 18th paragraph, appellant's petition, R. p. 627). Appellant in making this statement also overlooks the importance of stating fully and fairly all issues made by the pleadings of all parties. This Court should have been informed in that connection that appellees pleaded the Texas statute of four years' limitation, and that appellant's claim was stale and barred by laches, and on this issue the master found that appellant's notes were not sued on in the District Court of Dallas county, Texas, until April 30, 1889, and that they had never been renewed or extended, and that appellant under the second contract sold the rails to the Houston & Texas Central Railway Company, a year and ten months prior to the receivership in cause 185, three years and three months prior to the receivership in cause 198, and six years prior to the receivership in this cause, and that under the third contract it sold the rail under a contract dated sixteen months prior to the receivership in cause 185, two years and nine months prior to the receivership in cause 198, and five years and six months prior to the receivership in this cause. Appellant also omits to state that upon these issues and others presented by pleading and proof, the Court below found generally against appellant and dismissed its petition, and

filed no written opinion, and that appellant has appealed from said decree and assigns no errors attacking the decree appealed from, if based upon the issues made by the pleading and proof that the claim is stale and barred by limitation.

Appellant also fails to state that the case was heard by the trial court upon both the master's report and upon evidence (see decree, R. p. 681) that appellant filed no exceptions to the master's report, and has not brought up with the record the evidence either taken before the master or heard by the Court in connection with the report.

Second.—On pages 6 and 7 of appellant's brief we find a statement of what appellant's counsel conceive to be due on the second contract. On this subject the master finds as follows: "I find that 6.2 miles of the railway of the Waco and Northwestern division of the Houston & Texas Central Railway Company was laid with rails furnished under the first two above named contracts, *but no evidence was submitted to me showing what proportion of said rails were furnished under each of said contracts respectively.*" Appellant having made no effort to prove the facts as to the amount of rails laid on this 6.2 miles out of the first and second contracts respectively, and having filed no exceptions to the master's report, and without assigning any error, or laying any predicate for raising such a question in this Court, now coolly asks this court to go into an examination of that question. This Court will not assume the burden of patching up appellant's case by guessing at the number of rails laid down under the first and second contract on this 6.2 miles. Aside from this, under agreement of counsel made before the master, and by him reported to the Court, all rails under

the second contract (so far as these bondholders have any interest in that matter) are paid for by the 170 bonds hypothecated by the Houston & Texas Central Railway Company with the Lackawanna Iron & Coal Company as collateral security to the notes given for the balance due under the second contract. On this subject the master finds as follows: "It was agreed by counsel that without making any actual sale of the said 170 bonds the Court should consider the same as sold for said amount of \$157,250 on December 23, 1895, and should apply same as a credit as of said date, upon the claim of the Lackawanna Iron and Coal Company, or of the Southern Development Company, as the Court may determine." (R. p. 652).

It will be remembered that only \$118,000 remains unpaid on the second contract. Deducting the \$118,000 from the \$157,250 leaves an overpayment of \$39,250 out of the collateral security. The bondholders have the undoubted right to insist that the collateral security hypothecated shall be exhausted before the appellant would be allowed to go upon the common fund. In the case of *Thomas vs. Western Car Company*, 149 U. S., page 116, the Court say: "As a general rule, after property of an insolvent passes into the hands of a receiver or of an assignee in insolvency interest is not allowed on the claims against the funds. The delay in the distribution is the act of law; it is a necessary incident to the settlement of the estate." So that the Court could only deal with the principal sum due, and which is clearly shown to be overpaid nearly \$40,000.

Third.—Not having time to notice all the inaccuracies in appellant's brief, we pass to the consideration of what is said in the third, fourth, sixth, seventh, eighth, ninth, tenth,

eleventh and twelfth subdivisions, found on pages 18 to 21 inclusive.

Appellant's counsel states in the third subdivision, page 18, referring to these rails: * * * "by their use the railway of the defendant company was kept in safe running order, its business increased, its railway thereby rendered more valuable to the bondholders under the various mortgages thereupon, and especially to the bondholders under the deed of trust and mortgage sought to be foreclosed in the proceeding now before the Court." There is no warrant or authority in the findings of the master for such a statement as this. He does not in the remotest refer to the question as to what effect the placing of these rails had upon the business of the company, or whether it rendered the security more valuable to any of the bondholders.

It is true he finds that before and at the time the rail were purchased that the demand for new rail was practically imperative, etc., and that the rail were put in as fast as they arrived. But here the story ends abruptly. We hear nothing more on this subject. There is no intimation as to the effect of placing the rail in the roadbed had on the subsequent business of the company, whether its net income increased or diminished, or what effect if any the purchase and laying of this rail on thirty-seven miles of the Waco and Northwestern division had on the value of the bondholders' security. The fact is this subject is not in the remotest alluded to by the master.

We find in this same third subdivision this further statement: "The contracts were made and the rails furnished under the expectation and belief that they would be paid for out of the revenues and earnings of the property, and if

these were insufficient, out of the proceeds of sale thereof, but the defendant, instead of paying the debt due the Lackawanna Company out of the said earnings, used the earnings for the purpose of paying coupons upon the bonds secured by mortgage, upon which bonds the bill of foreclosure now before the court was filed." There is no warrant or authority for this statement in the findings of the master. The master finds on this subject as follows: "I find that when the aforesaid contracts were made with the said Lackawanna Company, both seller and buyer expected the debts to be paid from the *net* income of the railway." (R. p. 656.)

It will be seen from this finding that appellant did not expect any payment out of the gross or current revenues of the road, but only out of the net revenues. Chief Justice Waite, in the case of *Fosdick vs. Scholl*, thus defines net income: "The income out of which the mortgagee is to be paid is the net income obtained by deducting from the gross earnings what is required for necessary operating and managing expenses, proper equipment and useful improvements."

The distinction, therefore, is clear between gross and net revenues, and as appellant did not expect to be paid out of the gross or current revenues, but only out of the *net* revenue, its claim is, therefore, reduced to the level of general and floating debts. This finding of the master was not excepted to, and no assignment of error is predicated thereon. As to the latter portion of the above statement that the expectation was to be paid out of the proceeds of the sale of the property if the earnings were not sufficient, there is no warrant, except upon the unproved assertion to be found in appellant's petition. The master on this subject found: "That the credit extended under such contracts was at the

request of and for the accommodation of the defendant railway company and upon its general credit. That said sales were made without any stipulation that security should be given by the defendant company for said rails, or that payment therefor should be made out of any particular fund, or in any particular way. That said sales were for an unusually large amount of rails and the defendant was unable to pay cash therefor." (R. pp. 656-7.)

The assertion found in the above quotation, either in referring to the defendant railway company, or to the receivers, that they used the earnings for the purpose of paying coupons upon bonds secured by the mortgage, is also without any warrant or authority. On this subject the master finds: "I further find that the accounts of the railway company were not kept in such a manner as to indicate the exact fund out of which the interest on said first mortgage bonds of the Waco and Northwestern division were paid, or the exact fund out of which the interest upon the bonds of the other division was paid, and that no separate account was kept of the net earnings of said Waco and Northwestern division, as distinguished from the net earnings of the other divisions of said railway company either prior to or during the receivership thereof until April 20, 1889, or thereabouts." (R. p. 680.)

In the last portion of said subdivision 3, page 18, we find the following statement: "The rails were actually used for the betterment and improvement of the railway, and not for the purpose of construction." There is no warrant or authority in the findings of the master for this statement. He finds "that said sales were for an unusually large amount of rails," and he further finds "that the rails were placed in the

track of the defendant railway company as soon as received." (R. p. 657.) But he does not find or attempt to draw any such distinction as is made in this statement, but the inference is clearly deducible from his finding that the sales were for an unusually large amount of rails, that he considered the purchase as analogous to original construction, and was clearly a purchase on general merchandise account, and there is no other finding of fact on this subject.

Fourth—In the fourth subdivision, beginning at the bottom of page 18 and extending to page 19, we find the statement that the \$91,371 paid to the bondholders on the Waco and Northwestern division was paid before any proceedings whatever had been taken to impound the revenues of the defendant, or to affect them with any right whatsoever in favor of the bondholders. There is no warrant or authority whatever in the record to support this statement. The record shows that the first mortgage bondholders filed a general demurrer to the bill of the Southern Development Company, which was in May, 1886, in all things sustained, and cause 185 was dismissed, and receivers were appointed at the suit of the first mortgage bondholders on July 10, 1886, and said receivers held said property and net revenue by virtue of said appointment, and it was not until something like a year thereafter that the said \$91,371 was paid as interest on the bonds on the Waco and Northwestern division, and there is no warrant for the statement that the \$91,371 was paid out of the revenue of the railway. This is fully shown by the above quotation from the master, "that the accounts were not kept in such a manner as to indicate out of what funds these payments were made."

Fifth—In the seventh subdivision, on page 20 of appel-

lant's brief, we find that there was net revenue arising from the operation of the entire system by the receivers in cause 185, from February 23, 1885, to July 10, 1886, amounting to \$423,142.16, but there was no interest payment made out of this fund to the bondholders on the Waco and Northwestern division, nor has any of this fund ever come into the hands of the receiver in this cause, and none of the improvements, if any, erected out of said fund, or any funds in the hands of the receiver in cause 185, were put upon the Waco and Northwestern division. On this subject the master finds: "I find that no part of the income arising from the operation of the road, and no part of the proceeds of sales of old rails, old iron, old cars and engines, which was received by the receivers in causes Nos. 185 and 198, ever came into the possession of the receiver in this cause and the evidence fails to show that any part of the new equipments purchased by the receivers in causes Nos. 185 and 198, as shown above, ever came into the possession of the receiver in this cause. And the evidence fails to show that any improvements and betterments of the property added to the property of the Houston & Texas Central Railway Company, by the receivers in causes Nos. 185 and 198 were made on the Waco and Northwestern division." And further on he finds: "I find that the receivers in cause No. 185 had on hand in cash at the opening of business on January 21, 1886, \$175,393.65, but there is no evidence that any part of said fund came into the possession of the receiver in this cause. I find that the receiver in cause No. 198 had on hand at the beginning of business on April 6, 1889, cash amounting to \$215,842.54, but the evidence does not show that any part of said funds came into the hands of the receiver in this cause." The master finds and shows that the Waco and Northwestern di-

vision was operated as a part of the general system of the Houston & Texas Central Railway Company up to the time it was placed in the hands of a separate receiver on April 6, 1889, and his findings lead to the conclusion that a systematic method of favoritism was kept up during this entire time, appropriating the revenues of the Waco and North-western division without adding any betterments or paying any interest whatever upon the bonds held by the bond holders thereon. That these bond holders have received no interest whatever on these bonds for a period of over nine years, and for the same length of time only the sum of \$46,-505.40 was added thereto as betterments and permanent improvements, and that was done by the present receiver since December 10, 1892.

Sixth—The tenth subdivision found on page 21 is misleading and inaccurate, and we prefer that the Court would read the master's finding on this subject, and which has been quoted by us above.

This disposes of the most prominent inaccuracies that we have found in the brief for appellant. There may be others, but we have not time to point them out.

Seventh—On page 23 we find this statement in reference to appellant's method of presenting his assignments to this Court: "Instead of following the assignments of error closely, we think we can present the case more satisfactorily to the Court by discussing it in the manner in which we shall." The manner in which they do discuss this case is to invite a reconsideration of the whole case, with slightly any reference to the assignments of error, and a discussion of questions not raised, or in the remotest alluded to in any of

the assignments of error. We agree with counsel that they do not follow these assignments very closely, if at all. They start out with three propositions found on pages 23 and 24 of their brief, and while it may be barely possible that the first proposition is included in the broad, sweeping, general and inconclusive terms of appellant's assignments of error, propositions two and three found on page 24 not only have no application to the case, were not raised or presented in the lower Court, but are not in the remotest alluded to in their assignments of error, yet when they come to consider these questions they group together at the bottom of page 24 propositions one and two and ask this Court to consider the two together, when one of them is not raised by any assignment of error, and it is extremely doubtful that the other is.

We will first dispose of the second and third propositions found on page 24. It is therein asserted that the Farmers' Loan and Trust Company and the beneficiaries in the mortgage have never had a lien upon any of the earnings of the Waco and Northwestern division of the Houston and Texas Central Railway Company, and that they have no lien upon any such income now in the hands of the Court. The third proposition is that "if neither party has, nor at any time during this litigation has had, a lien on the income of the railway mortgaged in this case, then the Court will proceed upon the principle that equality is equity, and will distribute the income ratably among all of the creditors of the defendant railway company before the Court."

As stated above, neither of these propositions are included in any of the assignments of error, or was ever raised before in this case. The question for this court to determine is,

has appellant any charge or lien on the earnings of the Waco and Northwestern division of the Houston & Texas Central Railway Company? It is not material to this appeal to determine whether the bond holders have a lien on this fund.

But should this Court conclude to notice these propositions, we wish in that connection to refer to appellant's petition (R. p. 16), and the master's report thereon (R. p. 648). The subject is not in the remotest referred to in either, so far as we have been able to find, after a careful examination. But a sufficient answer to these arguments is that the record shows that the receiver in cause 227 was appointed on April 6, 1889, at the suit of the trustee in the mortgage. In such case it is not of the least importance whether there is any mortgage in existence. The appointment of the receiver, and his taking possession of the property, is an equitable levy on the income for the benefit of the moving party. This proposition is as old as the law of receiverships, and has never been doubted by any court within our knowledge, and is not disputed by appellant's counsel (see *Sage vs. Memphis & L. R. Ry. Co.*, 125 U. S., 40.) But the provisions of the mortgage is an equitable mortgage on the income, to be effective only when possession is taken after default. Such provisions are commonly and uniformly held to be effective as mortgages of the income after possession is taken (see *Stanton vs. Gay*, 86 Texas; 20 Am. and Eng. Ency. of Laws, p. —.)

The burden of proof was on the appellant to establish an equity in this revenue; having failed to do this, its petition was dismissed generally, without making any disposition of the revenue in the hands of the Court. There was no proposition either in the Court below or by the assignments of error to make pro rata distribution of the revenues among

the various creditors of the company, and we don't believe that this Court in the state of the record will enter upon the speculative investigation suggested by propositions 2 and 3. Propositions 2 and 3 being disposed of, leaves for consideration what is said by appellant in its first proposition, the substance of which is that it has in equity a charge on the continuing income of the railway both before and after the appointment of receivers, and that the Court should use the income in the way that the company would have been bound to use it in the discharge of appellant's debt, and that said income has been diverted from the payment of appellant's debt to the payment of mortgage creditors and the improvement of the mortgaged property, and to the extent of such depleted income appellant should be reimbursed out of the proceeds of sale of the mortgaged property. If we were certain that appellant would be content with this proposition, we could with more ease to ourselves proceed to the discussion of the question. It seems from this proposition that they confine their claim to the right to be reimbursed "out of the proceeds of sale of the mortgaged property," and does no longer contend that appellant is entitled to be reimbursed out of the net revenue in the hands of the Court. We presume from this abandonment that appellant is content that the fund be paid to Mr. Downs. We refer to the case of *Cutting vs. Tavares O. & A. R. Co.*, 61 Fed. Rep., at p. 156, opinion rendered by Judge Pardee. He says: "As the Court in appointing the receiver made no provision for the payment of said claims, and as there is no evidence in the record tending to show that the current earnings, either before or after the receiver was appointed, were diverted to paying unearned interest, or in fact any interest upon the bonded indebted-

ness, we are unable to sanction the order authorizing the payment of said claims from the proceeds of the sale of the property."

Appellant's counsel will not contend that there is a provision in any of the orders appointing receivers in any of the causes for the payment of back debts, and it is equally certain, though not conceded by appellant's counsel, that it has not been shown or found by the master, that any of the revenue, either before or after the appointment of the receiver, has been used for the erection of betterments or permanent improvements upon the Waco and Northwestern division, or for the payment of bonded indebtedness due on the bonds secured by the mortgage declared on herein.

We refer again to what the master says on this subject. He finds very distinctly "that the accounts were not kept in such a manner as to indicate the exact fund out of which the interest on said mortgage bonds on the Waco and Northwestern division were paid, or the exact fund out of which the interest upon the bonds of the other divisions were paid, there being no separate accounts kept."

In the case of *Kneeland vs. American Loan Company*, 136 U. S., page 97, it is said among other things: "It is the exception, and not the rule, that such priority liens can be displaced." The burden was upon appellant to prove that the improvements were erected on the Waco and Northwestern division and the interest paid on the bonds was paid out of the current income, in order to show a diversion and to establish the proposition contended for. No presumptions will be indulged by this Court in favor of appellant's case, and while the master finds that the receiver, Abeel, after December 10, 1892, and prior to September 3, 1895, ex-

pended \$46,505.40 for betterments and permanent improvements, he does not find that these improvements were erected out of the current income, or state out of what funds they were erected. (R. p. 663-4.) And these are the only improvements that have been erected on the Waco and Northwestern division of over eleven years, and they were erected nearly ten years after the rails were sold.

Eighth—Passing to page 26 of appellant's brief we find with some astonishment that counsel enters upon the general discussion of the question as to whether its claim was barred by laches. There is no assignment of error authorizing the presentation of this question by appellant. The complainant and these appellees specially pleaded that the claim was stale and barred by the Texas statute of limitation. On these issues, together with a large number of other issues presented in the case, the Court found generally against appellant, and could have very properly based its judgment upon the fact that the claim was stale and barred by limitation. But appellant has assigned no error complaining of the decree, if based upon these issues. This has been fully shown in our principal brief, and if the issues are fairly made and fairly supported by the testimony it is only necessary for this Court, in order to determine this appeal, to look to those issues, and if it is determined that it would not have been fundamental error for the Court below to decide the case on those points then it logically follows that the decree appealed from must be affirmed. Appellant does not say that it was erroneous to so render the decree.

Ninth—Counsel for appellant next takes up a large portion of its brief in extended quotations from the leading cases which have discussed questions of priority of various special

and limited claims over the mortgage bond holders, but in each and every one of these cases it will be found that the Court finds either that there was a diversion of the current revenue, used in paying either bonded indebtedness or the erection of permanent improvements, or that the claim allowed was found to be in fact a claim for current supplies needed from day to day, to keep the road a going concern, or some other special equity which addressed itself to the discretion of the chancellor in allowing the claim and giving it priority, but in this case there is no finding, and there is no fact by which it may be found by this Court that there has been any diversion of the current income to the erection of either improvements on the property or to the payment of bonded indebtedness, nor is it found that the rails were a part of the current expenses or current supplies needed to keep the road in operation from day to day as a going concern, but the inference is clearly to be drawn from the master's finding that this is a claim for general merchandise sold on the general credit of the company, and constitutes a part of its general floating indebtedness.

Without attempting to follow the argument of appellant or to review the cases cited, we beg to submit that the findings of the master and the law arising thereon sustains the decree appealed from upon all the following issues:

1. That the claim of the Lackawanna Company is a general or floating debt.

The master finds that the credit extended under these contracts was upon the "general credit" of the company. That "the sales were of an unusually large amount of rails, and the defendant was unable to pay cash therefor." The inference from this is that the company was unable to pay cash

because of this unusually large purchase. He finds that "the claim cannot be classed a current debt," that appellant only expected to be paid out of the "net income," and appellant alleges that it sold the rails relying upon the supposed existence of a clause in the mortgage providing for the payment of floating debts. On these facts the Court could have, and probably did, find appellant's claim to be one for general merchandise and a floating debt. But there is no assignment of error complaining of the decree if based on that ground. Debts of that character are never given priority.

Bound vs Ry. Co., 58 Fed. Rep., 480.

Thomas vs. Car Co., 149 U. S., 95.

Kneeland vs. Trust Company, 136 U. S., 89.

Note to case of Blair vs. Railway Company, 22 Fed. Rep., 478, note 2.

Before the decree will be reversed it must be shown by proper assignments of error that it can not be sustained on any of the defences urged against appellant's claim (Walker vs. Cole, 34 S. W. R., 713.)

2. That the debt is barred by the Texas statute of four years' limitation. This is fully shown on the merits under ninth proposition, pages — to — in these appellees' brief. That the issues of law and fact raised would have warranted the trial Court in deciding the case on those issues is there fully shown. That appellant does not by assignment of error complain of the decree if based thereon is fully shown on pages 9 and 10 of appellees' said brief.

3. That the debt is stale, in that the rail was sold too long prior to the appointment of receiver to be classed as a current debt for supplies. This fully shown on pages — to

— of the brief for appellees. There is no fixed or invariable rule on this subject. It must have been a reasonable time prior to the appointment of a receiver. What is a reasonable time is a question of fact (not of law, as stated in appellant's brief, page 34), and the trial Court having resolved that fact against appellant and held its claim to be barred by laches because the time was unreasonable, that action will not be reviewed by this Court in the absence of proper assignments of error complaining of the decree if based on that ground. There is no assignment of error which raises that question. The master finds that the rails delivered under the last contract were sold under a contract made sixteen months prior to the appointment of the receiver in cause No. 185, two years and nine months prior to the receivers in cause 198, and five years and six months prior to the receivers in this cause (R. p. 655). Whether or not this was a reasonable time was to be judged from the testimony. The trial judges may have and probably did conclude that this period was an unreasonable time. In the absence of an assignment of error this action is conclusive and not subject to review by this Court. The decree shows that the trial court heard the evidence in connection with the master's report (R. p. 681). Its conclusion on this question cannot be reviewed by this Court. Indeed, if it were necessary to do so to sustain the decree appealed from, it would be presumed that the trial court held the claim to be stale. This is so, because the decree is not complained of if based on that ground.

4. That there has been no diversion of the income to the payment of interest and the erection of improvements. This is fully shown on pages — of this supplemental brief, and pages — to — of the original brief, under fourth

proposition. There is no assignment of error complaining of the decree, if based on that ground. The third assignment of error states as a matter of fact in general terms that there has been a diversion, and complains only that the Court erred in not decreeing a restoration. But it does not complain that the Court erred in holding that there had been *no* diversion. The assignment assumes as a fact, independent of any ruling on that subject, that there had been a diversion of the income, but if the lower court differed with counsel, and found that there had not been, or that the evidence failed to show that there had been, its conclusion on that subject is binding on this Court, for it is not anywhere assigned as error. This being a Court of review it is not concerned so much with what are the facts, but what was found to be the facts, and what is complained of by the assignments of error. The trial court could not err in refusing a restoration until it had been determined that there had been a diversion. And not until it is complained of by an assignment of error that the Court erred in holding that there had been no diversion, will this Court review the question as to whether the Court erred in refusing to restore the fund.

5. That if petitioner has any equity it should be remitted to its intervention now pending in cause No. 198, which is a receivership covering the entire system. This is fully shown by the brief for these appellees on pages 22 to 28, under fifth proposition. This is what was practically done by the decree appealed from. Appellant's petition was dismissed without prejudice to its intervention in cause No. 198 (R. p. 681), and with this reservation, it is a difficult question to determine, unless the outside facts are known, just why this appeal is prosecuted so vigorously against a small

branch of the road. No error is assigned if the decree is based upon the ground that the rights of appellant, if any it has, must, under the facts reported by the master, be asserted in that cause.

6. That appellant in selling the rail relied upon the supposed existence of a provision in the mortgage requiring the payment of its claim, and did not expect to be paid out of the current income, but only out of the net income, and can assert claim in no other manner. Appellant alleges that it did sell the rail upon the faith of this mortgage, and the master finds that it expected to be paid out of the net revenue (see allegations in petition, R. p. 627, and findings of the master, R. p. 656). This allegation in connection with this finding of the master makes a case wherein appellant sued upon the mortgage claiming under the terms of an express contract made for its benefit. It failed, however, to prove its case. The Court could very properly and may have found against appellant on this ground. It certainly would not be a case of plain error to so find, for it could be nothing short of justice to give to appellant the full protection of its own contract and expectations thereunder. The allegation has never been modified or amended. No error is assigned complaining of the decree if based upon that ground.

We submit that nothing has been shown by appellant indicating that error exists in the decree appealed from, and we request that it be affirmed.

Respectfully submitted,

L. W. CAMPBELL,
*Solicitor for Appellees Moran Bros. and
Henry K. McHarg.*

10. 451. No. 2.

Brief of Turner for Respondents

Office Supreme Court, U. S.

FILED

JAMES H. MCKENNEY,
CLERK.

Filed Oct. 16, 1897.

Supreme Court of the United States,

OCTOBER TERM, 1897.

No. 451.

THE LACKAWANNA IRON AND COAL COMPANY
ET AL.,

Petitioners,

versus

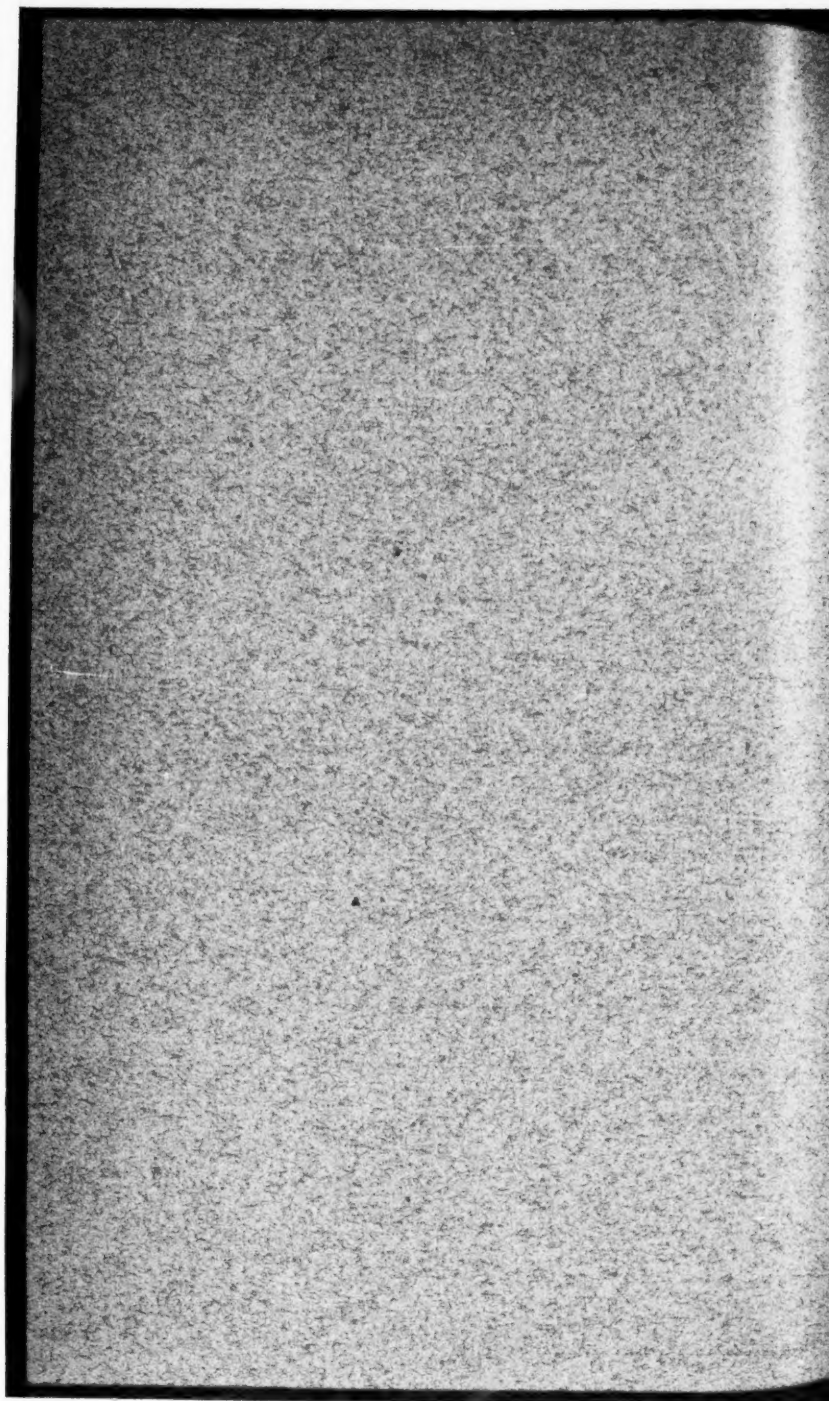
THE FARMERS' LOAN AND TRUST COMPANY ET AL.,

Respondents.

MEMORANDUM OF RESPONDENTS IN OPPOSITION
TO THE PETITION FOR A WRIT OF CERTIORARI.

HERBERT B. TURNER,

Of Counsel for the Respondents.



Supreme Court of the United States.

THE LACKAWANNA IRON AND
COAL COMPANY, *et al.*,
Petitioners,

vs.

THE FARMERS' LOAN AND TRUST
COMPANY *et al.*,
Respondents.

Memorandum of The Farmers' Loan and Trust Company in opposition to the petition for a writ of certiorari to the Circuit Court of Appeals for the Fifth Circuit.

This petition presents an extraordinary instance of the difficulties which stand in the way of holders of railroad securities in enforcing their liens. The matter now before the Court is an intervention of an unsecured creditor, the Lackawanna Iron and Coal Company, which had supplied the Houston and Texas Railway Company with steel rails and had accepted its notes in payment. A suit being brought by the Farmers' Loan and Trust Company, as trustee of a first mortgage covering the Waco branch of the Houston and Texas Central,

which mortgage was made a number of years before the purchase of the rails, this creditor intervened in that suit, claiming a lien prior to the lien of the mortgage.

The Houston and Texas Central Railway Company, a large Texas corporation, made several mortgages, one covering its main line in 1866, and others covering the branch lines from 1870 to 1877. There were several branch lines. One of these, called the Waco Branch, is the subject matter of the present litigation. On this particular branch the Houston and Texas Central placed two mortgages, a first and second, each to secure a separate series of bonds. The first is dated June 16th, 1873.

It is true, as the petitioner states, that prior to the bringing of the foreclosure suit in which this intervention was filed, there had been litigation affecting this entire railroad company, but this fact does not seem very material here. Receivers of the Houston and Texas Central Railway Company were appointed by the United States Circuit Court for the Eastern District of Texas in a creditor's bill filed by the Southern Development Company, claiming to be a creditor, in February, 1885. About one year afterwards, on May 27th, 1886, the Court dismissed the bill of the Southern Development Company on demurrer, but appointed new receivers on foreclosure bills, which were filed at that time by the holders of the first and second mortgages on the main line and Western Division. These bills were consolidated.

It must be carefully noted that the holders of the First Mortgage, Waco Division, bonds, secured by the mortgage under foreclosure in this cause, did not then file a bill to foreclose their mortgage, inasmuch as they considered their bonds perfectly good and a first-class investment at seven per cent. for a very considerable unexpired term. They discovered their error afterward.

A decree was had in the consolidated cause for the foreclosure of the mortgages covering the entire property on May 4th, 1888, and under the provisions of that decree the entire property was sold September 8th, 1888. The sale was made subject to the First Mortgage on the Waco Branch, which is the subject-matter of this suit. Indeed, the entire proceedings were subject to all rights existing under the Waco Branch First Mortgage.

After all this had happened, after the decree had been rendered and the sale had been made and the property had passed into the hands of the reorganized company, who took the same subject to the First Mortgage, Waco Division, the complainant, the Trustee under the First Mortgage, Waco Division, filed the bill in the present cause to foreclose its mortgage. It was filed April 6th, 1889.

It is not easy to see what the previous action, and the sale therein, has to do with this suit. The income of the entire property in the hands of the Receivers was devoted to the improvement of the railroad property, which was in such very bad condition that the line was popularly known as the "Angel Maker."

The complainant herein was first met by dilatory motions, which were not finally decided until October, 1890. Thereupon, the parties who had interposed these dilatory motions, and who represented the same interest as that represented by the petitioner in the present matter, demurred to the bill.

The demurrer was argued December 19th, 1890, and overruled a few days later. Thereupon, the defendants interposed an answer, which was filed on the February, 1891, rule day. Testimony was thereupon taken, with the usual delays, so that

the cause was not brought on for final hearing until March, 1892, and a decree of foreclosure and sale was rendered at that time. The decree contained the following provision respecting the claim of the petitioner, the Lackawanna Company :

“ IT IS FURTHER ORDERED, ADJUDGED AND DECREED, that the rights of the Lackawanna Coal and Iron Company * * * * intervenors herein, and the rights of all other intervenors herein, be and they are hereby reserved to be hereinafter adjudicated, and are in no manner affected or prejudiced by this decree. It is further ordered that the disposition of any surplus funds arising from the earnings of the road, or otherwise, that may be in the hands of the Receiver, is reserved for future determination.”

In accordance with this decree the property was sold December 28, 1892, and struck off to E. H. R. Green for one million three hundred and seventy-five thousand dollars.

Green did not complete his purchase. On the contrary, he took proceedings to be relieved of his bid. These proceedings occupied a great deal of time, and he was finally so relieved in 1894.

The property was thereupon again advertised for sale and sold September 3, 1895, for one million five hundred and five thousand dollars. Since then we have been ceaseless in our endeavors to compel the purchaser to complete his purchase, but hitherto without success.

Although the property has been sold and a responsible purchaser has bought it, and the sale, under the terms of the decree, is subject to this Lackawanna claim and the other claims which have been overruled by the Courts, nevertheless it seems impossible to have the sale completed so long as these claims are in litigation. It is understood that the purchaser represents the same interest which holds the claim of the Lackawanna Com-

pany. So that whether the claim is sustained as prior in lien to the mortgage or not would make no practical difference. Whether this protracted litigation can be still further prolonged may make a very considerable difference to the unfortunate bondholders who have had the singular experience of holding securities which, when the reorganization was effected a few years ago, were supposed to be worth par, but which now are almost unsalable, with interest overdue and unpaid for more than eleven years.

The petition for the writ of certiorari does not present questions of sufficient gravity and importance for the Supreme Court of the United States to require the Circuit Court of Appeals to certify this case to it for review.

The Supreme Court has already declared that it will only exercise this branch of its jurisdiction sparingly and with great caution, and never excepting in cases of gravity and importance. In the case of *Lau Ow Bew, Petitioner*, 141 U. S., 583, the Court, speaking through Mr. Chief Justice FULLER, said :

“It is evident that it is solely questions of gravity and importance that the Circuit Court of Appeals should certify to us for instruction ; and that it is only when such questions are involved that the power of this Court to require a case in which the judgment and decree of the Court of Appeals is made final, to be certified, can be properly invoked. The inquiry upon this application, therefore, is whether the matter is of sufficient importance in itself, and sufficiently open to controversy, to make it the duty of this Court to issue

the writ applied for in order that the case may be reviewed and determined as if brought here on appeal or writ of error."

In re Woods, 143 U. S., 202, this Court refused to grant a writ of *certiorari* on the ground that the questions were not of sufficient gravity and importance. Referring to the above case, the Court, again through Mr. Chief Justice FULLER, said :

"In the matter of *Lau Ow Bew*, the construction of acts of Congress in the light of treaties with a foreign government, and the status of domicile in respect of natives of one country domiciled in another, a matter of international concern, were brought under consideration upon the record, and we were of opinion that the grounds of the application were sufficient to call for our interposition.

But we do not regard the inquiry as to whether it was settled law in the State of Minnesota that a judgment of dismissal in a former suit, such as pleaded here, was not a bar to a second suit upon the same cause of action, or whether the law in respect of recovery by a servant against his master for injuries received in the course of his employment was properly applied on the trial of this case, as falling within the category of questions of such gravity and general importance as to require the review of the conclusions of the Circuit Court of Appeals in reference to them."

In *American Construction Company vs. Jacksonville Railway Company*, 148 U. S., 372, the plaintiff had filed a stockholders' bill against the defendant railroad company, praying for a Receiver. A Receiver was appointed and authorized to pay certain obligations of the railroad company out of the income coming into his hands and to borrow money on Receiver's notes for the same purpose. The railroad company appealed from the orders appointing the Receiver and authorizing the issue of Receiver's notes, and the Circuit Court of Appeals reversed and set aside both orders. This

Court, upon an application by the construction company for a writ of *certiorari*, refused the writ on the ground that the questions presented were not of sufficient importance.

In the course of the opinion by the Court, Mr. Justice GRAY used the following language :

“ In the same spirit, the authority conferred on this court by the very provision on which the petitioners mainly rely, by which it is enacted that ‘ in any such case as is hereinbefore made final in the Circuit Court of Appeals, it shall be competent for the Supreme Court to require, by *certiorari* or otherwise, any such case to be certified to the Supreme Court for its review and determination, with the same power and authority in the case as if it had been carried by appeal or writ of error to the Supreme Court,’ has been held to be a branch of its jurisdiction which should be exercised sparingly and with great caution, and only in cases of peculiar gravity and general importance, or in order to secure uniformity of decision. *Lau Ow Bew’s case*, 141 U. S., 583, and 144 U. S., 47 : *In Re Woods*, 143 U. S., 202. Accordingly, while there have been many applications to this Court for writs of *certiorari* to the Circuit Court of Appeals under this provision, two only have been granted ; the one in *Lau Ow Bew’s Case*, above cited, which involved a grave question of public international law, affecting the relations between the United States and a foreign country ; the other in *Fabre, Petitioner*, No. 1237 of the present term, an admiralty case, which presented an important question as to the rules of navigation, and in which the decree of the Circuit Court of Appeals for the Second Circuit reversed a decree of the District Judge, and was dissented from by one of the three Circuit Judges ; and in each of those cases the Circuit Court of Appeals had declined to certify the question to this Court.”

In the same opinion the Court further said that there were much stronger reasons against the interposition of the Supreme Court to review a de-

decree made by the Circuit Court of Appeals on appeal from an interlocutory order than in the case of a final decree.

"Clearly," said the Court, "this Court should not issue a writ of certiorari to review a decree of the Circuit Court of Appeals on appeal from an interlocutory order, unless it is necessary to prevent extraordinary inconvenience and embarrassment in the conduct of the cause."

And the same doctrine was reiterated in *Forsyth vs. Hammond*, 166 U. S., 514.

It is submitted that there is no question in the present case of sufficient gravity for the Supreme Court to review the decision of the Circuit Court of Appeals. The question upon this intervention was a purely private one, concerning no one except the parties immediately before the Court. It did not involve interests of any very great magnitude, nor issues of national importance. The claim was simply that of a contractor who, having supplied steel rails to the Houston & Texas Central Railway Company for construction purposes, and accepted notes for the payment thereof, maturing from time to time during several years, upon the insolvency of that company, sought to obtain for this unsecured debt a priority of lien over a mortgage which the railroad company had made to the Farmers' Loan & Trust Company.

In paragraph XXVIII the petitioners set forth what they regard as the two important questions of law involved in the cause. The first is as to the application of the doctrine of *Fosdick vs. Schall* to the present claim. This question was fully argued in the Court below, and a careful opinion (reported in 79 Federal Reports, 202), reviewing all

the authorities bearing on the subject was rendered. If this Court can be called upon to examine every claim for a priority of lien based upon the doctrine of *Fosdick vs. Schall*, then, to that extent, the object of the Act of 1891, creating the Circuit Court of Appeals, is frustrated. That act, as was said by this Court in *American Construction Co. vs. Jacksonville Railway*, cited above,

“Has uniformly been so construed and applied by this Court as to promote its general purpose of lessening the burden of litigation of this Court by transferring the appellate jurisdiction of large classes of cases to the Circuit Court of Appeals, and making the judgments of that Court final, except in extraordinary cases.”

The questions growing out of the case of *Fosdick vs. Schall* have for more than twenty-five years been the subject of controversy before every Circuit Court in the United States, as well as many of the State Courts, and have been the grounds of a multitude of appeals to the Supreme Court. The doctrine can no longer be regarded as in the least degree unsettled. In a series of long and careful decisions this Court has examined these questions in every aspect and has set forth in succinct form the rules applicable thereto. To aver (as the petitioners do), as a reason for this Court's interference that “This honorable Court has never yet in any case directly passed upon the questions constituting the distinguishing features of this case and controlling its correct decision,” is virtually to ask this Court to assume appellate jurisdiction in every instance where a claim is advanced under the shelter of *Fosdick vs. Schall*; for it would be difficult to conceive of such a claim which might not possibly be distinguished from those already brought to the attention of the Court, and for which, therefore, the

claimants might not assert some distinguishing feature as a ground for the Supreme Court's jurisdiction.

It is claimed by the petitioners in paragraph XXIX of their petition that the decision of the Circuit Court of Appeals for the Fourth Circuit, in a case entitled *Southern Railway Company vs. Carnegie Steel Company*, 76 Fed. Rep., 492, conflicts with and is in diametrical opposition to the decision of the Circuit Court of Appeals for the Fifth Circuit in the present cause, and that therefore the intervention of this Court is necessary in order to maintain a uniformity of jurisprudence between the different Circuit Courts of Appeals.

We submit, however, that the petitioners have misconstrued the remarks which the Supreme Court has made to the effect that a writ of *certiorari* will be granted where it is necessary to avoid a diversity of judgments. We think that a reference to the opinions of the Circuit Court of Appeals for the Fourth Circuit in the Carnegie Steel Company case, and of the Circuit Court of Appeals for the Fifth Circuit in this cause, will not disclose any different understanding by these two Courts of the principles that govern in such controversies. Both Courts carefully reviewed the decisions, particularly those of the Supreme Court, and applied the same doctrine to the respective state of facts before them. The claim in the one case was allowed and in the other denied; but that difference in result does not present a diversity of judgment which casts upon the Supreme Court the burden of review. The infinitely varying conditions which surround claims of intervenors in foreclosure suits will always give rise to differences in the application of the principles laid down by the Supreme Court. Even if this Court should issue the writ prayed for and, upon the

return of the writ, should reverse the decision of the Circuit Court of Appeals, it will not be pretended that Courts would never in the future deny a priority to those who had supplied steel rails to mortgaged railroads. The reason is that the diversity of judgment in this cause and the Carnegie Steel Company cause is not a diversity of *law*, but of *fact*, and that as long as the transactions of men differ there must necessarily be differences in the decisions of Courts of justice.

Upon the point suggested in paragraph XXVIII of the petition as the second important question of law involved in the cause, we have only to say that the matter there referred to falls largely within the arguments above suggested. Furthermore, that matter rested upon questions of fact as to the existence of any revenues in the hands of the Receiver peculiarly applicable to the payment of such claims as that of the petitioners, and the diversion of any such revenues to the use and for the benefit of the holders of the bonds secured by the mortgage foreclosed in this cause. These questions of fact must be treated as having been settled in the lower Courts adversely to the petitioners, and the Supreme Court cannot be asked to go into them now. It may be said in passing, however, that the attempt on the part of these petitioners to spell out a prior lien upon the revenues in the hands of the Receivers, being necessarily dependent upon the diversion to the benefit of the bondholders of current income applicable to the payment of petitioners' claim, it was primarily incumbent upon the petitioners to show that some such income was diverted. Far from showing this, however, they admit in the sixth paragraph of their petition that the receivership of the property in question did not arise until *nine months* after the last of the

rails supplied by them had been delivered to the railroad company. During all of this period (within which, if ever, the current income applicable to the payment of their claim must have arisen) the petitioners failed to enforce their claim, or to assert their right to any portion of the current income. On the contrary, as appears by the first and second paragraphs of the petition, they expressly waived any such right by taking notes, and renewals of notes, from the railroad company in lieu of payment, thus showing that they did not expect the current income to be applied to their use. And the last of the notes so taken matured subsequently to the appointment of the Receivers. Where, then, can the petitioners point to a diversion of income upon which to found a right to receivership revenues?

They state in paragraph XXVIII that the question here is whether a mortgagee has any lien upon the revenues of the mortgaged property accruing prior to the filing of a foreclosure bill, and during a receivership provoked by others; but, whatever view the Court might take of that point, the real question (if any there were), would be, not as to the lien of the *mortgagee*, but as to the lien of the *petitioners*. Their case must rest upon their own title, and not upon any alleged defects of the mortgagee's title.

For these reasons we submit that the petition for a writ of *certiorari* should be denied. We append hereto a copy of the brief which we filed in the lower Court.

HERBERT B. TURNER,
Of Counsel for the Respondent.

IN THE CIRCUIT COURT OF THE UNITED STATES,
FOR THE EASTERN DISTRICT OF TEXAS, AT
GALVESTON.

THE FARMERS' LOAN AND TRUST
COMPANY, Trustee,
Complainant,

vs.

No. 227 Eq.

HOUSTON & TEXAS CENTRAL RAIL-
WAY COMPANY, *et al.*,
Defendants.

*Interventions of the Lackawanna Iron & Coal Com-
pany, the Southern Development Company and the Mor-
gan's Louisiana & Texas Railroad and Steamship Com-
pany.*

**Argument for the complainant in opposi-
tion to said interventions.**

LACKAWANNA CASE.

Petition avers that under contracts of December 28, 1882, April 26, 1883, and of October 30, 1883, petitioner delivered to the Houston & Texas Central Railway Company about 18,000 tons of steel rails, and took therefor certain promissory notes of the Company, some of which were paid and some of which were extended; that all of said notes or extensions thereof were dated on or prior to December,

1884, and were past due at the time of the filing of the intervention herein, which was November 3, 1891. That said rails had been used in the betterment of the road, and were absolutely necessary, and alleges that the indebtedness was contracted by it in consideration of its promise to pay the same out of the earnings of its railway, and that they were furnished with the expectation and belief that they would be paid for out of the revenue and earnings. That the Houston & Texas Central Railway, with its branches, was placed in the hands of receivers on or about the 21st of February, 1885, and that when the bill was filed in this cause on the 6th of April, 1889, upon the first mortgage bonds, the receivership was extended in this cause; that a considerable portion of said rails (amount not given) was used upon the Waco & Northwestern Division, and that the intervention seeks to have the proportionate amount paid out of the earnings in the hands of the Receiver, or failing in that, out of the proceeds of sale.

The petition alleges that the Southern Development Company had brought suit upon a similar claim in the Federal Court in Equity Cause No. 185, to which general and special demurrers were filed and sustained by the Court and the bill dismissed without prejudice.

The contracts set out in the petition were referred to as part of the petition.

In his report filed herein on the 13th of January, 1896, the Master finds that negotiable promissory notes were given by the defendant company for all rails sold under the three contracts; that all of said sales were made on a stated credit for a fixed period of time, viz., six months after the average date of each delivery, and that said defendant company (the H. & T. C. Railway Company) had the right under said contracts to extend the time six months longer from the maturity of said notes; that such extensions were made for the accommodation and to suit the convenience of said defendant company, and that the said extended negotiable notes remaining unpaid matured in the months of February, March, April and May, 1885.

That all of the rails delivered under the first contract, and about one-half of the rails delivered under the second contract, were paid by the railway company prior to the appointment of any receiver of said property ; but that the remaining half under the second contract and all rails furnished under the third contract are not paid for.

That the rails furnished under the second contract were furnished under a contract made a year and ten months prior to the appointment of the receiver in Cause No. 185, and about three years and three months prior to the appointment of the receiver in Consolidated Cause No. 198, and about six years prior to the appointment of the receiver in this cause.

That the rails furnished under the third contract were furnished under a contract made about sixteen months prior to the receivership in Cause No. 185, and about two years and nine months prior to the receivership in Consolidated Cause No. 198, and about five years and six months prior to the appointment of the receiver in this cause.

He further finds as follows : " I find that the debt for which the Lackawanna Company claims payment in its petition herein cannot be classed as a current debt made in the ordinary course of business, as those terms seem generally to be understood, yet it appears that when the contracts hereinbefore mentioned were entered into between the said Lackawanna Company and the defendant railway company the condition of the track of the defendant railway company was such that the demand for new rails upon the most worn portions of the roadway was practically imperative."

And further, " I find that when the aforesaid contracts were made with the said Lackawanna Company, both seller and buyer expected the debts to be paid from the net income of the property ; that the credit extended under said contracts was at the request of and for the accommodation of the defendant railway company, and upon its

general credit. That such sales were made without any stipulation that security should be given by the defendant company for said rails, or that payment therefor should be made out of any particular fund, or in any particular way; that said sales were for an unusually large amount of rails, and the defendant was unable to pay cash therefor, and there was no way of obtaining said rails except upon a credit; and petitioner herein, at the time of said contracts and sales, had knowledge of the mortgage of June 16, 1873, given by the defendant company upon the properties of its Waco & Northwestern Division to secure the first mortgage bonds, which said mortgage has been herein foreclosed."

SOUTHERN DEVELOPMENT COMPANY CASE.

Petition alleges that the petitioner advanced to the H. & T. C. R'y Co. a large amount of money for moneys advanced by it to the defendant company to enable it to pay for supplies, labor, repairs, operating and managing expenses, proper equipment, useful improvement and other necessary expenses of its railway, by which defendant's railway had been kept in safe and running order. The dates of the advances are not given. Petitioner alleges that it filed suit in the Federal Court at Galveston, cause No. 185, and that upon general and special demurrers being interposed same were sustained and the bill was dismissed without prejudice. It alleges that part of said advancements went to the benefit of the W. & N. W. Division, and seeks to recover the proportionate part in this case out of the earnings in the hands of the receiver, or from the proceeds of sale.

The Master finds that the money was *loaned* to the defendant company by the Southern Development Company and sums up the purposes for which it was used in general terms as follows: "I find that by the advances so made by petitioner to said defendant railway company the railways of said defendant company were kept in safer running order, and its property and business increased and rendered more valuable to the bondholders under the

mortgage described in the bill of complaint filed in this cause, as also to all other creditors of the defendant railway company; that said advances were so made to defendant railway company for the purposes aforesaid, and without them said company would not have been able to maintain its credit and meet its obligations, and that said advances were made in consideration of the promise of the defendant railway company to pay the same." The said advances were made between the 14th of July, 1884, and March 24, 1885.

MORGAN CASE.

Petition alleges an indebtedness on account of certain promissory notes, dated respectively in the years 1882, 1883 and 1884, for money loaned the H. & T. C. R'y Co. for improvement, equipment and betterment of its road, to purchase supplies, pay for labor, etc. Alleges the bringing of the suit by the Southern Development Company, No. 185, the interposition of demurrers, the sustaining of the same, the dismissal of the bill on the 27th of May, 1886, without prejudice. Alleges that the loans were made to the H. & T. C. R'y Co. in consideration of its promising to pay the same out of the earnings of its railway, and alleges an equitable lien superior in rank to the mortgage bonds and coupons. That a portion of said money was used for the benefit of the Waco & N. W. Division, and seeks to recover the proportionate part of said indebtedness out of the earnings in the hands of the receiver or out of the proceeds of sale.

The Master finds that between December 9, 1880, and the 26th of May, 1884, the defendant company executed and delivered to the Morgans' Louisiana and Texas Railroad and Steamship Company, intervenor, sundry promissory notes for moneys advanced to it by intervenor; and further finds as follows:

"I find that during the year 1884, and for several years prior thereto the finances of the defendant company were in an embarrassed condition, its expenses, in-

cluding fixed charges, interest, etc., exceeded its income for the year 1871, \$670,839.14 ; 1882, \$430,177.16 ; 1883, \$570,979.25 ; 1884, \$991,481.44 ; and it reasonably appears that without the advances made by petitioner as herein recited (constituting nearly one-third of its floating debt as it existed in 1884), it would not have been able to maintain its credit and meet its obligations.

“ I find that by the advances so made by petitioner to said defendant railway company the railways of the defendant company were kept in safe running order and its property and business increased and rendered more valuable to the bondholders under the mortgage described in the bill of complaint filed in this cause, and also to all other creditors of the defendant railway company ; that said advances were so made to defendant railway company for the purposes aforesaid, and that without them said company would not have been able to maintain its credit and meet its obligations, and that said advances were made in consideration of the promises of the defendant railway company to pay the same.”

Argument.

It is submitted that the petitions for intervention do not make out a case of contract or statutory lien. We do not understand that this character of lien is seriously claimed, and the findings of the Master conclusively settle this question against the interventions. The laws of the State of Texas then in force permitted railroads to borrow money and to mortgage their property, but prescribed the mode and manner in which mortgages might be executed, and rendered them invalid unless such laws had been complied with. The Act of 1876, as given by articles in Sayles' Texas Civil Statutes, prescribes :

“ Art. 4219—Right to borrow money, issue bonds, etc.
—Such corporation shall have the right from time to time to borrow such sums of money as may be necessary for con-

structing, completing, improving, or operating its railway, and to issue and dispose of its bonds for any amount so borrowed, and to mortgage its corporate property and franchises to secure the payment of any debt contracted by such corporation for the purposes aforesaid.

"ART. 4220—Mortgage invalid unless, etc.—No mortgage by such corporation shall be valid unless authorized by a resolution adopted by a vote of two-thirds of all the stock of such company, after notice and in a manner provided in this title for increasing the capital stock of such corporation.

"ART. 4221—Resolution authorizing mortgage shall be recorded—When any such resolution has been adopted, in the manner provided by the preceding article, it shall be recorded in the office of the Secretary of State, and no such resolution shall take effect until so recorded."

The H. & T. C. Ry. Co. is a corporation created by and existing under the laws of the State of Texas, and is bound by all the provisions and restrictions of the General Railroad Act. No mortgage or lien can be created by contract unless in the mode prescribed by the statute, and there is no pretense that this has been done. The intervenors must, therefore, either stand upon the usual claim of equitable lien against the net earnings or upon some statutory lien. No statutory lien is shown by their petitions. The question arises, have they any equitable liens? Where one furnishes iron to be laid into a railroad and allows it to go into and become a part of the road, it is covered by such mortgage and he has no lien which can displace it.

G. H. & H. *vs.* Cowdrey, 11 Wall., 459.

N. O. & O. R. R. Co. *vs.* Mellen, 12 Wall., 362.

A railway mortgage upon present and future acquired property of a railway company, and its incomes and profits, is a prior lien only upon the net earnings of the road after the payment of all the operating expenses, where the road is in possession of the company.

Hale *vs.* Frost, 99 U. S., 389.

Section 584, of Jones on Corporate Bonds and Mortgages, says :

"It has sometimes been sought to establish equities in favor of those who have furnished material or money for completing or repairing of railroads, on the ground that the property has thus been conserved and rendered capable of a profitable use. This is, in fact, an attempt to apply to railroads the principle adopted by the civil and maritime laws of awarding priority to the last creditors who furnish necessary supplies and repairs to a vessel. Thus, in *Galveston, etc., R. R. vs. Cowdry*, the person who had furnished the iron laid upon a portion of the road claimed therefor an equitable lien in preference to an existing mortgage : First, because the mortgage covered the iron only as future acquired property, and upon the principle of equitable estoppel, which should yield when it comes in conflict with a superior equity ; and, secondly, because his property, applied to the road, had rendered it capable of being operated when it otherwise could not have been used. The Supreme Court of the United States denied the claim on both points, declaring that the mortgage attached to the property as soon as it was acquired, and that the principle of the maritime law contended for had no application."

The case of *Blair vs. St. Louis, etc., R. R.*, 23 Fed. Rep., 521, held that an attorney was not entitled to a preference over the mortgage as regards money paid by him upon judgments against the railroad company and upon claims for wages and for stock killed, under an agreement that the amount so advanced should be repaid by the company though the payments were so made by him within six months before the payment of a receiver. He simply loaned the money to the railroad company without security. If he had taken a mortgage at the time of making the loan he could not have claimed priority of payment over an existing mortgage.

Under the authority of 29 Fed. Rep., 561 ; 20 Fed. Rep., 260 ; 33 Fed. Rep., 778 ; 22 Fed. Rep., 179 ; 22

Fed. Rep., 471, and 5 Fed. Rep., 846, the principle is adduced that the equitable lien in favor of creditors (even if one exists) who have furnished labor and supplies is not allowed to extend back for a longer period than six months, except under extraordinary circumstances. In fixing this period the Courts recognized the principle that the extent to which this class of claims has to run back is measured by the usual course of credit and business of the company in the conduct of its affairs—that is, the usual term of credit upon which companies have purchased their supplies, or settled, as in the case of railroads, with their connecting lines, is taken as the measure of the period within which this class of claims shall be protected.

We submit to the Court that no case is stated in any of the petitions for intervention giving the intervenors any standing or entitling them to any relief in a court of equity.

Jurisdiction in these cases must be founded, because the petitioners' claims are of that equitable character that gives them a standing for remedy and relief in a court of equity, or because of some special character of the defendant as a railway company, and such conditions and acts of the defendant shown in the petition as to entitle them to come into a court of equity for relief against the railroad company.

FIRST—*As to the intervenors' claims.*

Not contesting at present the most equitable completion that can be desired for their claims—that is, for necessary indispensable supplies for the operation of the railroad contracted in good faith on the expectation of payment out of the current earnings at the time they accrued—it is, we believe, without example or precedent, that such claims have ever been the foundation of a proceeding in equity. They are mere debts, simple contract debts, not a lien or privilege affixed to anything for which remedy can be claimed in a chancery court. Until the decision of *Fosdick vs. Schall*, 99 U. S., in 1878, and the

contemporary and subsequent cases we hazard nothing in asserting that no lawyer ever dreamed of going into equity with such claims. It is not suggested in any treatise on equity, any book on liens, or contracts or receivers. In no case were they ever sustained. In *Railway Co. vs. Cowdry*, 11 Wall., 482, the Court, by Justice Bradley, had said: "As to the point of giving priority to the last creditor for aiding to conserve the thing, all that is necessary to say is, that the rule referred to has never been introduced into our laws except in maritime cases which stand on a particular reason."

And in recent years the United States Supreme Court has more than once repeated this statement that the doctrine of maritime liens cannot apply to railroads.

Thompson vs. Valley R. R. Co., 132 U. S., 68.

Fogg vs. Blair, 133 U. S., 534.

Toledo R. R. Co. vs. Hamilton, 134 U. S., 296.

In *Trustees vs. R. R. Co.*, 2 Wood, 542, 1876, Justice Woods had said: "The fact that the floating debt was contracted in good faith for the benefit of the railroad company's property, and therefore for the benefit of the bondholders, is true perhaps of all such debts. But that does not give the floating debt creditors any ground upon which to claim that their debt should be paid first * * * To undertake to do it would be to invade the legal rights of the bondholders, and, if established, as within the power of a court of equity, would shake the credit of railroad securities throughout the world."

In *Denison vs. R. R. Co.*, 4 Biss., 416, 1864, Judge Drummond said: "What equitable lien had these petitioners for materials furnished a railroad on that fund? None. Why? Because those who had prior liens came in and swept it away; and more than that had not been half paid. It is precisely like the case of a man who furnishes to the owner of a farm the means of carrying it on; but

there is another party who has a lien upon the farm, and it is sold and ordered that the party may be paid. Now the fact that the mechanic or laborer has furnished the means of carrying on the farm would not authorize him to come into a court of equity and cut off the prior lien which exists on the farm and prevent it from being paid. These parties ought to be paid. They have a just claim against the road, but it is against an insolvent corporation and they ask parties who have a prior right and lien to pay them because those with whom they had dealt cannot."

High, on Receivers, sec. 394a, lays down the rule that mere contract debts of a railway company as for labor, materials and supplies incurred prior to the appointment of the receiver, and unsecured by any lien upon the property, cannot be given priority over antecedent mortgages; and the proposition that such contract debts can through the aid of a court of equity be given such priority seems to be a proposition wholly indefensible upon sound reasoning.

The present petitions are an experiment at a novel, unjust and unauthorized extension and perversion of the doctrine of *Fosdick vs. Schall*, and kindred cases, to go far beyond the principles of those decisions, and in fact to revolutionize the primary elements and most settled doctrines of equity jurisprudence and practice.

The principle of *Fosdick vs. Schall* is clear and it is this: It was a suit by the mortgagee, in which he applied for and obtained a receiver, a condition of which, imposed by the Court at the appointing of the receiver, was that the receiver should pay out of the current earnings all debts due and owing for labor and services rendered in operating the railroad within the last three months, and all indebtedness of engines, iron, wood, supplies, cars or other property purchased within the said period of three months for the use of the company. Certain cars were used by the road prior and subsequent to the appointment of the receiver, and for rent for the use of the cars prior to the

appointment of the receiver. Schall claimed priority to the mortgage out of the proceeds of the sale of the mortgaged property. The Supreme Court rejected his claim, and we shall have further occasion to compare this claim to the claims of the intervenors when we come to define the precise character of the latter; but the Chief Justice took occasion to lay down the doctrines on which allowances could be rightfully made out of the earnings in the receiver's hands, or out of the proceeds of the sale of the mortgaged property. This opinion was evidently made on great consideration, and has been since repeatedly recognized by the Court. We only seek at present to ascertain from the case the exact nature of the legal right or claim of those creditors for necessary materials who are declared entitled to preference by the Court. It held that, even though the mortgage may in terms give a lien on the profits and income, until possession is actually taken, or something equivalent done, the whole earnings belong to the company and are subject to its control. That the mortgagee has strict rights which he may enforce in an ordinary way. If he asks no favors he need grant none; but if he calls upon a court of chancery to put forth its extraordinary powers and grant him purely equitable relief, he may with propriety be required to submit to the operation of a rule which always applies in such cases and do equity in order to get equity. The appointment of a receiver is not a matter of strict right. Such application always calls for the exercise of judicial discretion, and the Chancellor should so mould his order that, while favoring one, injustice is not done to another. If this cannot be accomplished the application should, ordinarily, be denied; also, that if no such order is made when the receiver is appointed, and it appears from the progress of the cause that bonded interest has been paid, additional equipment provided, or lasting and valuable improvements made out of the earnings, which ought in equity to have been employed to keep down debts for labor, supplies and the like, it is within the power of the Court to use the income of receiverships to discharge obligations which, but for the diversion of the fund, would

have been paid in the ordinary course of business. This not because the creditors to whom such debts are due have in law a lien upon the mortgaged property or the income, but because, in a sense, the officers of the company are trustees of the earnings for the benefit of the different classes of creditors and the stockholders; and if they give to one class of creditors that which properly belongs to another the Court may, upon an adjustment of account, so use the income which comes into his own hands as if practicable to restore the parties to their original equitable rights.

Here is expressed positive determination that the creditors for necessary supplies have no lien on the mortgaged property or on the earnings; that the earnings, until possession, obtained of them by the mortgagee, in accordance with his strict legal right, notwithstanding the mortgage lien, "belong to the company, and are under its control." The company is, in a sense, a trustee of all creditors and stockholders to act fairly and equitably with its earnings. If, in the right of the mortgage, he obtains a receiver, the Court, as the condition of the favor of the equity it extends to him, will compel equity to be done to the current-fund creditors.

Now nothing can be less doubtful than that the Court lays down no possible doctrine from which it can be justly argued that the current-fund creditor has any lien in law, and it is obvious that he meant equity law, not law as contradistinguished from equity, authorizing him to proceed against the earnings of the *corpus* of the property. No one could have said more plainly than the Chief Justice, if he had wanted to, that the current earnings creditor has a prior lien to the mortgage creditor, and is entitled for its enforcement to the same remedy in equity that the mortgage creditor possesses for his lien. If such had been the principle, the theory, the philosophy of the opinion, so carefully matured and expressed, and intended for precedent, it would have been made clear; but, instead of this, and to the reverse of this, the nature of the right of the current-earnings creditor is most carefully

guarded by "sound judicial discretion, which may, under the circumstances of the particular case, appear to be reasonable"; an equity growing out of the doing of equity, in order to get equity by the mortgagee, dependent upon the most general "sense" of "trust" in which the officers of a corporation are trustees for all its creditors and stockholders.

The mortgagee has his entrance into equity by virtue of his mortgage. The mere simple contract creditor never had, and has not now, any standing to go into a court of equity. This doctrine is too elementary to require discussion or authority; otherwise all distinction between law and equity as to railroads would be obliterated.

The case of *Express Company vs. Railroad Company*, 99 U. S., 191, decided at the same term as *Fosdick vs. Schall*, throws the strongest light on this branch of the case. The Express Company advanced \$20,000 to the railroad company to be expended in repairing and equipping its railroad, for which it was to have certain express facilities, accounts to be made monthly, and to continue for a year, and until payment of the \$20,000. The railroad company then executed a deed of trust to secure mortgage bonds, and foreclosure suit was brought and a receiver appointed. The receiver refused to complete the contract, and the Express Company sued in equity for its performance, which, of course, involved compensation therefor. Mr. Justice Swayne said: "The appellant has no lien. * * * As well might the receiver be decreed to satisfy the appellant's demand by money as by the service sought to be enforced. Both belong to the lienholders and neither can be thus divested. The appellant therefore can have no *locus standi* in a court of equity. Both those objections appear by its own showing. It was therefore competent for the court below *sua sponte* to dismiss the bill for want of equity apparent on its face."

Hale vs. Frost, 99 U. S., 389, decided by the Chief Justice at same term, was a case where the mortgagee, after default of two years on interest, obtained a receiver, who

made net earnings over and above all operating expenses, and the question was payment out of those earnings to the mortgagee, or to an intervenor for supplies for machinery to the company, which went into the possession and use of the receiver. The ruling is that the net earnings made by the receiver are not necessarily the property of the mortgagee, but are subject to the disposal of the Chancellor in the payment of claims which have superior equities, which that of the intervenor had in that case.

Turner vs. Railway Company, 8 Biss., 315, decided in October, 1878, by Judge Drummond, was a review of the rulings of his circuit on this class of claims, after the fullest argument, and immediately preceded *Fosdick vs. Schall*, and laid down the law in identical terms. The Judge said: "During the discussions which have taken place on this subject, the allowance of these back claims has been sometimes called a lien, but in point of fact it never has been nor can it be justly so called, but, as already stated, is an exercise of the equitable power of the court in the premises."

Miltenberger vs. Railroad, 106 U. S., 286, decided in 1882 by Justice Blatchford, was a case where default on the first mortgage occurred November, 1873, on the second mortgage January, 1874, and suit for foreclosure brought by the mortgagee August, 1874. A receiver was appointed, with directions to pay the arrears due for operating expenses incurred within ninety days, and to pay not exceeding ten thousand dollars to competing lines and for materials and for repairs and ticket and freight balances; also to make certain improvements and purchases, and this was sustained.

The question at once suggests itself, why limit the amount to ten thousand dollars, or the time to ninety days, if such claims have a legal standing constituting right or cause of action? A few extracts from the opinion will show how variant was the principle on which the Court proceeded from the idea of the existence of any such right or ground of action:

"It cannot be affirmed that no item which accrued before the appointment of a receiver can be allowed in any case. Many circumstances may exist which may make it necessary and indispensable to the business of the road and the preservation of the property for the receiver to pay pre-existing debts of certain classes out of the earnings of the receivership, or even the *corpus* of the property, under the order of the Court, with a priority of lien. Yet the discretion to do so should be exercised with very great care. The payment of such debts stands *prima facie* on a different basis from the payment of claims arising under the receivership, while it may be brought within the principle of the latter by special circumstances. It is easy to see that the payment of unpaid debts for operating expenses, accrued within the ninety days, due by a railroad company suddenly deprived of the control of its property, due to operatives in its employ, whose cessation from work simultaneously is to be deprecated in the interests both of the property and of the public, and the payment of limited amounts due to other and connecting lines of road for materials and repairs, for unpaid ticket and freight balances, the outcome of indispensable business relations, where a stoppage of the continuance of such business relations would be a probable result in case of non-payment, the general consequence, involving also largely the interests and accommodations of travel and traffic, may well place such payments in the category of payments to preserve the mortgaged property in a large sense by maintaining the good will and integrity of the enterprise, and entitle them to be made a first lien."

It is clear that no idea was in the mind of the Court that those claims or any of them, prior to the receivership, when they accrued by virtue of any contract right, or of their own inherent, legal or equitable force, were liens upon the property, or could have judicial standing to be asserted as such. They were claims, debts, which from the beneficial effect of so doing, in preserving the railroad property, advancing the success or interests of the receivership, it became equitable, with reference to the receivership itself, to pay, and therefore the Court gave

them priority of payment. The term lien is alone used as the result of the priority allowed by the Court under the special circumstances of the receivership. If they possessed legal standing, why limit the aggregate allowance of them to the arbitrary amount of ten thousand dollars or to the period of ninety days? The receiver had put the payment of this class of claims on the ground that "it was indispensable to the business of the road, and unless authorized to provide for them at once the business of the road would suffer great detriment. These reasons were satisfactory to the Court." Some of the claims were expressly disallowed although "the creditors threatened not to furnish any more supplies on credit unless they were paid the arrears," and the court says "the action sanctioned by the Court in allowing claims within the scope of the order of the Court appears to have been careful, discriminating and judicial."

When a mortgagee, entitled to relief in equity, solicits or obtains the appointment of a receiver, the judicial wisdom and necessity of considering all the equity and policy as respects the interests of the receivership and the principles of justice of the payment of any particular claim, is apparent. The situation furnishes its own reasons and its own law. But that the holder of a claim, not in itself a lien, not of its own right entitled to any standing in a court of equity, can be permitted to force its way into equity, obtain a receiver, and then make the receivership furnish the ground of the equity of his claim, seems to us extremely absurd.

The Trust Company *vs.* Souther, 107 U. S., 591, arose where default was made on the mortgage interest October 1, 1873, and semi-annually thereafter. December 6, 1879, the mortgagee filed bill of foreclosure and obtained a receiver, the order for which required the receiver to pay and discharge all amounts due and owing for labor or supplies accrued in the operation and maintenance of the road within six months immediately preceding. The net earnings of the receivership exceeded \$200,000, which with the assent of the mortgagee was expended in pur-

chasing additional grounds and rolling-stock and making permanent improvements of the railroad, all of which was embraced in the sale, leaving about \$65,000 of debts unpaid, of the character which the Receiver had been ordered to pay, and the question was upon their right to payment out of the proceeds of sale. The Chief Justice said that their right to such payment is decided by *Fosdick vs. Schall and Miltenberger vs. Railroad Company*. The principle of the decision as applied to the particular case ought to be quoted :

“Prior to the appointment of the receiver the gross earnings do not appear to have been enough to pay expenses, but afterward they yielded a considerable surplus. There cannot be any doubt that it was to the interest of the bondholders that the road should be kept in operation, and as they did not see fit to take possession while it could only be operated at a loss, it certainly was not an abuse of judicial discretion for the Court to order, as a condition of granting their application for a receiver, that the debts incurred by the company in thus protecting their security should be paid from the income of the receivership if in consequence of an increase of revenue it could be done.”

It was then held that, as those net earnings, instead of being applied to pay the debts as directed, were, by the request of the mortgagee, diverted to add to the value of the mortgaged property, afterward sold, with no intention of the Court to revoke the original order, the proceeds of sale would, in equity, be held to represent the fund directed to be applied to the labor and supply creditors when the receiver was appointed.

Burnham vs. Bowen, 111 U. S., 776, decided by the Chief Justice—Mortgage executed June 1, 1871, to secure bonds for \$4,125,000; no interest was ever paid, the company remaining in possession and operating the road until 1875, when a suit for foreclosure was commenced, a receiver was appointed, and the receivership earned over \$25,000 of net earnings. All of which, together with the

railroad, went into the hands of the mortgagee, by strict foreclosure, but subject to the claim of Bowen, amounting to \$6,515.42 for coal sold to the railroad company in 1874—"one of the current debts for operating expenses, made in the ordinary course of a continuing business, to be paid out of the current earnings," and there was no other liability on account of current expenses unprovided for when the receiver took possession, and this claim would have been paid out of current earnings, at maturity, had the Court not interfered, at the instance of the trustees, for the protection of the mortgage creditors.

Out of his earnings the receiver had paid \$7,898, a debt for real estate for the company, and nearly \$18,000 for right of way. The court held that the right of Bowen for payment out of the earnings by the receiver, was within the principle of *Fosdick vs. Schall*, those earnings having been diverted to payment for additional property to increase the security of the mortgage debt. But the opinion declares: "We do not now hold any more than we did in *Fosdick vs. Schall*, or *Huidekoper vs. Locomotive Works*, 99 U. S., 258, 260, that the income of a railroad, in the hands of a receiver for the benefit of mortgage creditors who have a lien upon it under their mortgage, can be taken away from them and used to pay the general creditors of the road. All we then decided, and all we now decide, is, that if current earnings are used for the benefit of mortgage creditors, before current expenses are paid, the mortgage security is chargeable in equity with the restoration of the fund which has been thus improperly applied to their use."

These decisions by the Supreme Court of the United States seem to us to leave no ground to doubt that the claim of a creditor for supplies, etc., admitted in the fullest sense to come within the class specified by Chief Justice Waite of "Current Income creditors," has no such lien within the purview of equity law as entitles him to a standing in a court of equity by original suit for its assertion and enforcement.

In *Coe vs. Railroad Company*, 31 N. J. Eq., 105, the Court thus construes *Fosdick vs. Schall*: "The grounds on which the decision rests are the power of the Court to do equity, in the imposition of equitable terms, at the time when its aid is invoked by the mortgagee for the realization of the money due him on his security."

In *F. L. & T. Co. vs. M. & R. Co.*, 21 Fed. R., 261, the nature and right to the relief is clearly shown by Love, D. J.: "It is not necessary to the right of intervention to participate in a trust fund, in *custodia legis*, that the intervenor should first obtain a judgment at law, or that he should have any lien upon the fund."

In *Douglass vs. Cline*, 12 Bush's Ky. R., 608, the claim of employee, etc., on current earnings, is placed within the equitable control and discretion of the Court as to such earnings.

In *Dow vs. R. R. Co.*, 20 Fed. Rep., 260, 188, an able Federal Judge, while giving the fullest weight to the principles of the Supreme Court decisions, and providing, in the appointment of a receiver on the application of the mortgage creditor, for payment of the labor and material creditors, in a case in which there had been delay of a year by the mortgagee to apply for a receiver, uses this language: "It is no answer to say that the company used its earnings for other purposes. The bondholders knew such liabilities must be incurred in running the road. They had it in their power to take possession of the road and secure its earnings and pay such liabilities. The class of persons protected by this order could not do anything to protect themselves, or compel a different application of the earnings."

Why not? Why could not these current-fund creditors do anything to protect themselves, or be heard, as to the application of the earnings? Because they had no lien upon the earnings, no right of action or suit which attached to or fixed itself upon them. No standing to go into a court of equity and say that these earnings were

mortgaged, hypothecated, pledged to them ; that they had any form or manner of privilege or hold thereto, or thereon, for which they could ask the relief or decree of a court. It did not enter into the remotest imagination of the careful and able Judge, in giving the utmost latitude to the letter and spirit of the decisions of the Supreme Court on this subject, that the current-fund creditors had not only a right of action to come into a court of equity and assert a superior paramount lien on the earnings, but, far beyond this, to obtain the helping hand of the Court through its extraordinary and powerful instrumentality to take possession of the road and all its property, sequester all earnings on hand, use and apply future earnings indefinitely, repair, reconstruct, renovate the tracks, lay steel rails, build bridges, construct round-houses, etc., and all for the purpose of making earnings so as to create and make priority of payment to the current fund creditors.

Another case in which an able Federal Judge has endeavored to define the nature and status of the claims of the creditors preferred for payment out of the earnings on the appointment of a mortgagee receivership will throw additional light upon this question.

Blair *vs.* Railway Company, 22 Fed. Rep., 471, November, 1884, Judge Brewer said :

“ What claims are entitled to such equitable preference ? The Master has reported in favor of all claims accruing since the default in payment of interest on the mortgage debt—a period of over two years. This seems to proceed upon the assumption that the mortgagees, failing to take action, have made the mortgagor company their agent to incur debts—have impliedly consented that all such debts shall take preference of their secured claims. I do not think that this principle is sound. There is no implied agency to that extent, and I do not think that the rulings of the Supreme Court are based upon any such doctrine. The idea which underlies them I take to be this : That the management of a large business like that of a railroad company cannot be conducted on a cash basis. Temporary credit

in the nature of things is indispensable. Its employees cannot be paid every month. It cannot settle with other roads its traffic balances every day. Time to adjust and settle these matters is indispensable. Because in the nature of things this is so such temporary credits must be taken as assented to by the mortgagees, because both the mortgagees and the public are interested in keeping up the road and having it preserved as a going concern; and whatever is necessary to accomplish this result must be taken as assented to by the mortgagees. In this view, such temporary credit accruing prior to the appointment of the Receiver must be recognized by the mortgagees and the claims preferred. Now, for what time prior to the appointment of a receiver may these claims be sustained? There is no arbitrary time prescribed, and it should only be such reasonable time as in the nature of things and in the ordinary course of business would be sufficient to have such claims settled and paid. Six months is the longest time I have noticed as given. Ordinarily I think this is ample. Perhaps in some large concerns with extensive lines of road, and a complicated business, a longer time might be necessary. Certainly so far as the present road is concerned six months is ample. If any person permits a claim to continue a longer time than that he certainly has no right to be considered other than a general creditor with no preference on a secured debt. * * * Out of what shall these claims be paid? Primarily, of course, out of the earnings of the road, and ordinarily out of such earnings alone. * * * This is fair, because if no receiver were appointed and the claimants attempted by legal process to enforce the collection of their claims they could obtain no priority over the mortgages, but must still be subject to such mortgages. So that the appointment of a receiver ought not to give them a priority which they had not before."

He says that cases may arise in which such claims should be made a lien on the corpus of the property, but this is only in exceptional cases, and on special equity which must be shown.

The nature of this class of creditors is thus distinctly shown by Judge Brewer to be merely a simple contract debt, on credit, to be paid out of the earnings promptly in the ordinary course of the business of the company. The mortgagee, whose debt is in default, impliedly assents to such payment, and if the mortgagee obtains a receivership before the ordinary and proper time for such payment had elapsed, if to be made in due course of business, the Court, out of the net earnings of the receivership, should make the payment. But such debts standing beyond the period in which there was sufficient opportunity for payment out of the current earnings, if the current earnings had been adequate and so applied, are general debts, alone, with no equitable claim to any preference whatever.

The entire want of any character of lien to become the foundation of a suit in equity, as against the earnings, or the corpus of the property, of the claims which are the foundation of the petitions of the intervenors, is manifest from the entire body of decisions on this subject, and is expressly shown wherever the true equitable nature and status of such claims has received any definition at the hands of a court. It has never been asserted by any judge or in any book.

The argument heretofore has proceeded upon a line showing that the claims propounded by the intervenors would have no foundation in equity if original bills had been brought upon them.

In the next place, we submit that the claims of the intervenors are not of a character which under a receivership obtained by the mortgagees would entitle them to any equitable preference, but they are of the direct contrary character, and are wholly without equity.

The petitioners do not show the intervenors to be creditors within any period of time giving them preference.

It is to be observed that in *Fosdick vs. Schall* the order appointing the Receiver required payment of all debts for

labor, supplies, engines, iron, cars, etc., incurred within three months before the appointment. In *Miltenberger vs. Railway Company* it was limited to payment for arrears of operating expenses and for other classes of debts not exceeding ten thousand dollars accrued within ninety days. In *Union Trust Company vs. Souther*, to six months preceding the appointment of the receiver. In *Burnham vs. Bowen* there was but a single debt contracted but a short time before the receivership and which would have been paid at the day by the company but for the receivership. In *Trust Company vs. Midland Company* payments were limited to six months before the appointment of receiver. The language and reasoning of the Court is to be applied to the state of facts here existing. We submit that the correct analysis of them has been made and the true principle deduced by Judge Brewer in 22 Fed. Rep., from which we have already quite fully quoted. That is the true import of the language of the Chief Justice in *Burnham vs. Bowen*, 111 U. S., 783: "We do not now hold any more than we did in *Fosdick vs. Schall* or *Heidekoper vs. Locomotive Works*, 99 U. S., 258, that the income of a railroad in the hands of a receiver for the benefit of mortgage creditors who have a lien upon it under their mortgage can be taken away from them and used to pay the general creditors of the road. All we then decided, and all we now decide, is that if current earnings are used for the benefit of mortgage creditors before current expenses are paid the mortgage security is chargeable, in equity, with the restoration of the fund which has been thus improperly applied to their use."

That is to say; the only case which can arise against the mortgagees is as to current expenses and current earnings. Not old debts contracted months or years ago for then current expenses. The soundness is manifest of the observation of Mr. Justice Wood, 2 Woods, 542: "The fact that the floating debt was contracted in good faith for the benefit of the company's property, and therefore for the benefit of the bondholders, is true perhaps of all such debts." It is scarcely conceivable otherwise. Its general debts must

be of that character or they would be ultra vires and illegal. But it is a debt current when the receiver is appointed to which alone the equity attaches.

In *Barry vs. Railway Company*, 27 Fed. Rep., 1, Judge Wallace held, where a mortgage was given for the payment of semi-annual interest out of the net earnings of the railroad, that the expenses defrayed or incurred in producing earnings for a given interest period are the only charges that can enter into the income accounts for that period, except payment of interest on prior incumbrances; and that indebtedness contracted prior to such interest period cannot be charged against its net earnings so as to prevent the mortgagee from claiming his interest.

The debt of the Lackawanna Company was simply a contract debt for steel rails furnished to the Houston and Texas Central Railway at a given price per ton, for which the railway company was to give its notes at six months, with a privilege of extension of an additional six months. Not a word said in the contract how the debt was to be paid. Nothing said in the contracts about the earnings or any attempted lien thereon. Only a finding that the parties expected the notes at the dates of their last maturity to be paid out of the earnings. The other two cases are for money loaned upon the credit of the railway company to keep it a going concern. The debts contracted more than twelve months before the Central Railway with its branches was placed in the hands of a Receiver in the original cause of the Southern Development Company, and nearly six years before the bill was filed in this cause and the receivership extended thereunder. According to our understanding there is not a single fact which would bring them within the purview of the principle announced in *Fosdick vs. Schall*, even with that principle extended to the most radical extreme. The Lackawanna Company sells rails to the Houston and Texas Central Railway upon a credit of six months, with the privilege of extension for six months longer. The Southern Development Company, being a California corporation, lends money to a Texas railroad company to buy its supplies, etc., and upon similar

facts the Morgan Company files its petition. And for these they claim a lien superior to the mortgagees as against the net earnings and corpus of the property.

Preference of payment in *Fosdick vs. Schall*, was given to debts due and owing for labor and services rendered in operating the railroad and for engines, wood, supplies, cars, or other property purchased within three months and the class of debts to which the Court attributes the implied agreement of the mortgagee for preference is the current debts made in the ordinary course of business. In the *Miltenberger* case the order to the Receiver was to pay arrears due for operating expenses within ninety days and indebtedness not exceeding ten thousand dollars for materials and repairs, ticket and passage balances, and to connecting lines within ninety days. In the *Souther* case it was for coal which would have been paid for when due but for the receivership. This is the class of indebtedness upon which the equity allowed by the court against mortgagees arises. It is limited to such cases and not to be extended to others not within the same reason and policy.

In *Fosdick vs. Schall* certain railroad cars were purchased conditionally by the railroad and used by the company six months before and also during the receivership. The Supreme Court allowed for the use during the receivership, but decided that the prior rent for use of the cars constituted no equitable claim against the *prima facie* right of the mortgagees.

In the *Huidekoper* case, certain locomotives were sold to the railroad company to be paid for at stated periods, title to be in the vendor until payment made. The Court gave the Receiver authority to return the engines and to adjust, settle and pay for their use during the receivership. The Master reported an amount for that payment. The Court said: "The railroad company contracted to buy the engines and pay a certain price. The locomotive company retained a paramount lien to secure the sum so to be paid. The debt so incurred was not paid. The lien has been in effect foreclosed, and the balance of the debt

still remains due. Whatever may have been the form, this is the substance of the transaction. No equitable claim upon any fund in Court has been established as security for this debt. The locomotive occupies the position of a general creditor with no special equities in its favor."

In *Hale vs. Frost*, 99 U. S., 389, preference was allowed to so much of a claim as was for supplies for machinery but was rejected for materials for construction.

In *Express Company vs. Railroad Company*, 99 U. S., the former loaned the latter \$20,000, to be expended in repairs and equipments for said road and the Supreme Court decided that there was no standing in equity for the balance of this sum due.

In *S Bissell*, 315, in which Judge Drummond defines the equitable discretion of the Court in dealing with property of the peculiar character of a railroad, it is to require receivers to pay operatives and supply men.

Judge Caldwell, 20 Fed. Rep., 267, defines them as persons furnishing labor and supplies and material for the use of the road.

Judge Brown, 22 Fed. Rep., 471, says: Claims for labor and supplies.

In *Douglas vs. Cline*, 12 Bush, 608, a preference was for back pay to employees for wages.

In *L. C. & N. Company vs. Railroad Company*, 29 N. J. Eq., 252, the railroad being involved made a bargain with a contractor, who was to furnish it with labor and services on the railroad. The Court held that such contractor had no equity against the mortgagees.

In *Catheron vs. Railroad Company*, 14 Fed. Rep., the preference is for amounts due employees and for supplies and materials.

In *re Kelly*, 5 Fed. Rep., 846, money advanced by the Lackawanna Company to the railroad company for neces-

sary uses, increasing the security of the bondholders at the request of some of the bondholders, and whilst the company was in default on its interest, held not to give a preference over bondholders obtaining receivership.

In *Blair vs. Railroad Company*, 23 Fed. Rep., 521, Justice Brewer says: "The attorney of the road paid off sundry judgments rendered against it, paid certain claims for wages and for stock, and paid them under an arrangement between himself and the President of the Company that the money thus advanced by him should be repaid on the 1st of January, 1884. This was only a few weeks before the appointment of a Receiver, and his claim is, that having paid these liabilities of the company at its instance, under a contract by which repayment was to be made to him within less than six months before the appointment of a Receiver, such debt should be preferred to the mortgage; we do not think so. It simply amounts to this: He loaned the company so much money but the bondholders had loaned theirs long before and loaned it secured by a lien. If he had taken a mortgage at the time of making this loan and thus obtained a lien, no one would contend that he thereby obtained priority over the earlier loan. This is all this transaction amounts to. He loaned to such company but did not take a lien. Now he asks that not having taken a lien and having loaned the money a few weeks before the appointment of a Receiver that he should obtain priority over those who loaned money three or four years or more ago and then took a mortgage."

In *Bridge Company vs. Douglas*, 12 Bush, 673, money borrowed to pay interest on coupons held not entitled to payment out of earnings. It did not stand in the place or have the equities of the coupons themselves.

Bound vs. Railway Company, 58 Fed. Rep., 473, Oct. 4, 1893, steel rails to the amount of over \$50,000 necessary for the maintenance of the road were purchased in April, 1888, by the railway company upon credit of eight months from the Lackawanna Iron and Coal Company,

This purchase was made 18 months prior to the appointment of a Receiver. The expectation and promise of the president of the railway company was that the purchase would be paid for out of the earnings of the railroad. This promise and expectation was not fulfilled and only a portion of the debt was paid, the notes for the balance being extended from time to time until the Receiver was appointed. During this interval in July, 1888, three months after the purchase of the steel rails, and before the first note matured the sum of over \$33,000 was paid on account of interest to the second consolidated mortgage bondholders. The Chief Justice, acting as Circuit Justice, and Hughes and Morris, District Judges, composed the Court, the opinion being rendered by Judge Morris, who said: "The rule giving preference to current expenses incurred on the faith of the earnings of a railroad shortly before the appointment of a Receiver has never been carried so far. The debt of the Lackawanna Company was an ordinary merchandise debt, evidenced by notes which were renewed from time to time. * * * The railroad company being heavily mortgaged, all that any unsecured creditors had to look to for payment was the earnings. The immediate earnings, it is clear, the Lackawanna Company did not look to, as the sale was upon a credit of eight months. * * * The claim is quite different from those ordinary and necessary current expenses of operating railroads, contracted but a short time before a receivership, and which, by the sudden action of the Court in appointing a Receiver, are left unpaid." And in reference to the promise which the president of the railroad made to pay the debt out of the earnings, the Court said: "In the present case it is true that the promise was to pay out of the earnings, and it is also true that out of those earnings to the extent of the amount decreed to have priority interest was paid to the second mortgage bondholders; but it is also true that by granting a credit of eight months, and by extending that credit over a period amounting in all to eighteen months, the Lackawanna Company must have contemplated that the interest falling due on the mortgage bonds was to be kept paid out of the earnings,

so that the road could remain in the hands of the railway corporation." And the Court disallowed the priority of that claim over any of the mortgage bonds.

In the case of *Kneeland vs. Trust Company* 136 U. S., 89, the Supreme Court uses this language: "No one is bound to sell to a railroad company or to work for them, and whoever has dealings with a company whose property is mortgaged must be assumed to have dealt with it on the faith of its personal responsibility and not in expectation of subsequently displacing the priority of the mortgage lien. It is the exception and not the rule that such priority of liens can be displaced. We emphasize this fact of the sacredness of contract liens for the reason that there seems to be growing an idea that the Chancellor, in the exercise of his equitable powers, has unlimited discretion in this matter of the displacement of vested liens."

We close our citation of authorities upon this branch of the case by reference to *Thomas vs. Car Company*, 149 U. S., 95, in which the Supreme Court circumscribed the bounds within which an equity court should confine itself in allowing any unsecured claim to displace vested contract liens. Wages due employees, current operating expenses, current balances of ticket and freight money, arising from indispensable business relations, and similar current debts accruing within ninety days are recognized as among the limited class of claims which, in its discretion, the Court may allow to have priority. The Supreme Court held it was error to allow a claim for the rental of cars necessary to operate the road for six months prior to the receivership; and said: "The case of a corporation for the manufacture and sale of cars dealing with a railroad company, whose road is subject to a mortgage securing outstanding bonds is very different from that of workmen and employees, or those who furnish from day to day supplies necessary for the maintenance of the railroad; such a company must be regarded as contracting upon the responsibility of the railroad company, and not in reliance on the interposition of a court of equity."

We undertake to say, with absolute confidence, that no case can be produced in which any Chancellor appointing a receiver has included among the claims which he has specified for prior payment claims for money loaned to the railroad.

On the contrary, in the year 1890, the Supreme Court of the United States, deciding the case of Morgan's, etc., Company *vs.* Texas Central Railway Company (137 U. S., 171), must be taken as having set this question forever at rest. In that case the Texas Central Railway Company had executed two mortgages to the Farmers' Loan and Trust Company as Trustee in 1879 and 1881 respectively. In 1884, it had executed another mortgage to another Trustee. Default occurred under the first two mortgages in May, 1885. The Houston and Texas Central Railway Company, operating the Texas Central, had been making advances to the latter from time to time on a running account, and in November, 1884, took demand notes of the Texas Central Company for the amount of these advances, which notes were afterward pledged to the Morgan Company. The advances had been made for operating expenses, taxes, etc., but had been applied by the Texas Central Company to the payment of coupons upon its first mortgage bonds. In April, 1885, the Morgan Company brought suit and had a Receiver of the Texas Central Company appointed, amending its bill in May after default had been made in the mortgages, so as to make the mortgage Trustees parties and claiming priority for the notes of 1884. The Trustee answered and subsequently filed a cross-bill for foreclosure. The Court absolutely denied the priority of the Houston and Texas Central advances in accordance with the doctrines laid down in its prior decisions. The following remarks occur in the course of the opinion :

" If the advances can therefore be treated as having been specifically procured for, or specifically applied to the payment of interest on said bonds (although there is no evidence to that effect), still such payment would

afford no basis for the assertion of a preference as against the bondholders. * * *

The contention is wholly inadmissible that the bondholders, because they received what was due them, should be held to have assented to the running of the road at the risk of returning the money thus paid, if the Company by reason of unrealized expectations, on the part of those who made the advances, should ultimately turn out to be insolvent and unable to go on. * * *

The doctrine of *Fosdick vs. Schall*, 99 U. S., 235, is that a court of equity may make it a condition of the issue of an order for the appointment of a receiver, that certain outstanding debts of the Company shall be paid from the income that may be collected by the receiver, or from the proceeds of sale; that the property being in the hands of the Court for administration as a trust fund for the payment of incumbrances, the Court, in putting it in condition for sale, may, if needed recognize the claims of material-men and laborers, and some few others of a similar nature, accruing for a brief period prior to its intervention, where current earnings have been used by the Company to pay mortgage debt or improve the property, instead of to pay current expenses, under circumstances raising an equity for their restoration."

This case is but a reiteration of the principles established in the Court's preceding decisions. It holds that even had there been such a diversion of the income to the benefit of bondholders as would have entitled material-men to an equitable priority, yet a money-lender did not come within the class of preferred claimants. The case is marked by a disposition to narrow the field of these ever-increasing claims for priority. The Court attacks with considerable severity the attitude assumed by some under the supposed shelter of the *Miltenberger* case that the public nature of railroad corporations absolves them in some mysterious way from fulfilling their private obligations to the purchasers of their bonds.

"It is true," says the learned Chief Justice in his able opinion, "that a railroad company is a corporation

operating a public highway, but it does not follow that the discharge of its public releases it from amenability for its private obligations. If it cannot keep up and maintain its road in a suitable condition and perform the public services for which it was endowed with its faculties and franchises, it must give way to those who can. Its bonds cannot be confiscated because it lacks self-sustaining ability, to allow another corporation, which, for its own purposes, has kept a railroad in operation in the hands of the original company by enabling it to prevent those who would otherwise be entitled to take it, from doing so, a preference in reimbursement over the latter on the ground of superiority of equity, would be to permit the speculative action of third parties to defeat contract obligations, and to concede a power over the property of others which even governmental sovereignty cannot exercise without limitation. And if all these advances should be considered as applied in payment of the operating expenses only, upon the theory, where such was not literally the fact, that they supplied a deficit created by the payment of interest out of the gross earnings, the same remarks would be applicable."

In all the statutory lien laws which have been enacted in this country with reference to railroads, buildings of every kind, and agricultural liens, we undertake to say that none has ever given a lien for loans of money. The views of legislators and of judges on this subject have grown out of public policy, arising from the necessity of protection and justice to the class of persons mentioned in all the above decisions—laborers, employees, men who supply materials necessary to the actual daily use and consumption of the road. There is no such equity in behalf of the money lender. He needs no such protection. Almost a compulsory necessity binds the dealing of the employee and supply men with railroad companies. It is their daily business—subsistence dependent upon it—and credit for short periods essential to the daily transactions. Not so with the money lender. No such considerations compel him to lend his money to the railroad company. He stands at arms' length. He goes for his profit. Instead of being the victim of the subject of necessity he is a seeker-out for the necessity of others, and

obtains advantage from them. We appeal not to prejudice, but simply state facts, which courts are quickest to declare as inherent in the very essence of equity.

What could be more infinitely dangerous and disastrous than to recognize as preference claims loans of money to railroad companies? When an order is made to pay for labor and supplies received within a certain period, it explains itself, and involves the equity on which it is founded, and which the Court intends to protect. But if this should be extended to money lending to the railroad, for the general purpose of paying for labor, supplies, operating expenses, etc., all safeguard, all certainty and security are gone. As was said in *2 Woods*, 542, that is the real character, perhaps, of all such debts.

We now come to consider the bill and the provisions of the mortgage under which the proceedings in this suit were instituted. The mortgage was dated in 1873, and while in the granting clause the earnings of the road are not specifically mentioned it is clearly inferable that the same are to be applied to the payment of the interest after default declared and possession taken. For convenience of reference we make the following quotation :

“ And in case the said Houston and Texas Central Railway Company shall fail to pay the principal or any part thereof, or any installment of interest or any part thereof on any of the said bonds at any time when the same shall become due and payable according to the tenor thereof and for sixty days after having been demanded, it shall be competent for said Trustee, its successors or assigns, to enter upon the said railway and the premises and property herein conveyed, by its attorneys and agents, and take possession of the same, without let or hindrance of the said first party, and every part and parcel thereof, and the appurtenances, and appoint an agent to operate and manage the same and receive the revenue and income thereof, applying the said fund after deducting taxes, necessary expenses and counsel fees, to keep the same in good order and repair, and the surplus to pay the interest and princi-

pal of all bonds which may be due and outstanding and secured hereby *pro rata*, and thereafter to the payment of any contributions due to the sinking fund herein established. And upon the request of the holders of one-fifth in amount of the bonds so in default which may be at any time outstanding under this deed of trust, it shall be the duty of said second party, by its president or agent duly appointed in its behalf to enter upon and take actual possession with or without entry or foreclosure, of said railway and property herein described, and all and singular each and every part and parcel thereof, and assume its management until the arrears of both principal and interest be paid or the property sold as herein prescribed, receiving the rents, revenues and income thereof and applying them in the same manner as above stated."

The bill was filed April 6, 1889, alleged default in payment of interest due on the 1st day of January, 1886, and of every installment which has fallen due since that day; alleges accelerated maturity of bonds, and seeks foreclosure and sale.

The property had been placed in the hands of receivers in Equity Causes Nos. 185 and 198; and on the date of the filing of the bill the same receiver was appointed in this cause and the receivership extended herein.

It will be borne in mind that after the receivership in Nos. 195 and 198 on the main line, including all of its divisions, the interest until the 1st day of January, 1886, was paid, when the default first occurred, and the *corpus* of the property was then in the custody of the court. Sixty days thereafter the Trustee had the right of entry, but it could not exercise that right because of the condition of the property. It filed its bill in April, 1889, when the receivership was extended in the present cause, but never for one moment during the interval had the Court released that custody. The final decree in this cause finds that a very large amount of interest was due at the date of its rendition. We claim that we are entitled to have the net earnings which accrued before the institution of this suit

applied to the payment of that interest. We think we have very conclusively shown that the net earnings which have accrued since that time belong to us and upon this latter proposition we think there can be no serious controversy. Otherwise our mortgage security would be seriously impaired. The contention that the intervenors are entitled to be paid out of the *corpus* of the property, in our opinion, is not entitled to serious consideration.

The nature of railroad bonds and their importance in the business and finances of the country are well recognized. Payment of interest gives them value, causes them to command good prices, to be sought after, to circulate freely; they are instruments of the very highest negotiability. The courts have been jealous of their protection against defenses of which notice could not be fully imputed to their holders. And yet the argument here is, that the purchaser of a railroad bond takes it subject to be docked in favor of floating debt creditors and the decree of an equity court giving a paramount lien on the *corpus* of their mortgage property in favor of all such floating debt creditors together with the further claim that they are entitled to all of the net earnings. Mortal ingenuity could not stamp such securities with greater confusion, distrust and ruin. The purchaser of each bond would be at the peril of an *ex post facto* equity suit to determine the floating debt in existence. We contend that no court has ever so decided. It is impossible in the very nature of right and wrong.

M. F. MOTT,
TURNER, McCLURE & ROLSTON,
For Complainant.

No. 162, 22

FEB 27 1899

JAMES H. McLAUGHLIN
Clerk

By. of Turner & Mott for Appellant

Supreme Court of the United States,

OCTOBER TERM, 1898.

Filed Feb. 27, 1899.

NO. 162.

THE LACKAWANNA IRON AND COAL COMPANY,
Intervening Petitioner-Appellant,

vs.

THE FARMERS' LOAN AND TRUST COMPANY,
Complainant-Respondent.

BRIEF FOR THE FARMERS' LOAN AND TRUST COMPANY,
RESPONDENT, IN OPPOSITION TO THE INTERVENTION
OF THE LACKAWANNA IRON AND COAL COMPANY.

HERBERT B. TURNER,
M. F. MOTT,

*Solicitors and of Counsel for THE
FARMERS' LOAN AND TRUST COMPANY.*

Supreme Court of the United States,

OCTOBER TERM, 1898.

THE LACKAWANNA IRON AND
COAL COMPANY, Petitioner,
Intervenor-Appellant,

vs.

THE FARMERS' LOAN AND TRUST
COMPANY,
Complainant-Respondent.

Brief for the Farmers' Loan and Trust Company, Respondent.

Statement.

In 1866, and prior to that time, The Houston and Texas Central Railway Company was a Texas corporation, operating a railroad from the north line of that State to Houston, with a branch from Houston to Austin, and another branch from Bremond to Waco. It made a mortgage covering the main line in 1866, and subsequently other mortgages covering the branch lines respectively, besides several junior mortgages. One of these branches, called the Waco and Northwestern Division, is the subject-matter of the present litigation. On this particular branch the Houston and Texas Central placed two mortgages, a first and a second, each to secure a separate series of bonds. The first is dated

June 16th, 1873. The suit in which the Lackawanna Iron and Coal Company filed its intervention was brought by the Farmers' Loan and Trust Company, as Trustee, to foreclose this first mortgagee.

Several years before this foreclosure was commenced, and in February, 1885, Receivers of the entire property of the Houston and Texas Central Railway Company, including the Waco and Northwestern Division, were appointed by the United States Circuit Court for the Eastern District of Texas, under a creditor's bill, filed by the Southern Development Company, which claimed to be a creditor for moneys loaned, etc. The cause instituted by the Southern Development Company was known as Cause No. 185. A little more than one year after its institution, and in May, 1886, the Court, Mr. Justice Woods of this Court presiding, dismissed the bill of the Southern Development Company, on demurrers filed by James Rintoul and Nelson S. Easton, the main line first mortgage trustees. Thereupon, and on the day of the dismissal of said bill, the trustees of the mortgages on the main line and on the Austin Division filed bills to foreclose those mortgages, and the causes were consolidated under the title of Consolidated Cause No. 198, and James Rintoul, Nelson S. Easton and Charles Dillingham were appointed Receivers under such foreclosure bills.

It must be carefully noted that the trustee of the first mortgage on the Waco and Northwestern Division, which is the mortgage to foreclose which the present suit was brought, did not then file a bill to foreclose that mortgage, the holders of those bonds being under the impression that they were a perfectly good seven per cent. investment, with a very considerable time to run. They discovered their error afterwards.

A decree was had in Consolidated Cause No. 198 for the foreclosure of the mortgages covering the entire property, on May 4th, 1888, and under the provisions of that decree the entire property was sold September 8th, 1888. The sale was made subject to the first mortgage on the Waco and Northwestern Division, which is the subject-matter of this suit. Indeed, the entire proceedings were subject to all rights existing under the Waco and Northwestern first mortgage. That division was sold separately, subject to the first mortgage, and purchased by one George S. Downs.

On September 6th, 1889, and after all this had happened, after the decree had been rendered and the sale had been made and the property had passed into the hands of the reorganized company, which took the same subject to the first mortgage on the Waco and Northwestern Division, the complainant, the trustee under that first mortgage on that division, filed the bill to foreclose the same. This suit became known as Cause No. 227, and a Receiver was appointed therein.

The complainant was first met by dilatory motions, which were not finally decided until October, 1890. Thereupon, the parties who had interposed these dilatory motions, demurred to the bill.

The demurrer was argued December 19th, 1890, and overruled a few days later. Thereupon the defendants interposed an answer, which was filed on the February, 1891, rule day. Testimony was taken, with the usual delays, so that the cause was not brought on for final hearing until March, 1892, when a decree of foreclosure and sale was rendered. The decree contained the following provision respecting the claim of the petitioner, the Lackawanna Company:

"It is further ordered, adjudged and decreed, that the rights of the Lackawanna Coal and Iron

Company * * * intervenors herein, and the rights of all other intervenors herein, be and they are hereby reserved to be hereinafter adjudicated, and are in no manner affected or prejudiced by this decree."

In accordance with this decree the property was sold December 28th, 1892, and struck off to E. H. R. Green for one million three hundred and seventy-five thousand dollars.

Green did not complete his purchase. On the contrary, he took proceedings to be relieved of his bid. These proceedings occupied a great deal of time, and he was finally so relieved in 1894.

The property was thereupon again advertised for sale and sold September 3d, 1895, for \$1,505,000.

The intervening petition of the Lackawanna Iron and Coal Company (Transcript of Record, page 75) avers that on the 28th day of December, 1882, the 26th day of April, 1883, and the 30th day of October, 1883, under three certain contracts bearing said dates, the petitioner agreed to furnish to the Houston and Texas Central Railway Company, upon terms and conditions specifically set forth in said contracts, about 20,000 tons of steel rails, at the prices severally mentioned; that it was agreed in said contracts that upon the delivery of each 560 tons of said rails, or thereabouts, payments were to be made to the petitioner therefor in cash, or in notes of the railway company, payable in six months from the average date of delivery to the maturity of the notes, with interest at six per cent., and with the privilege of renewing the notes before their maturity for a further term of six months; that under the first contract of December 28th, 1882, petitioner delivered about 5,020 tons of rail, and received therefor under the contract ten

promissory notes, and that under the second contract of April 26th, 1883, the petitioner delivered about 5,009 tons of rail and received promissory notes, and that under the third contract of October 30th, 1883, petitioner delivered about 8,552 tons and received promissory notes, all of which were extended for six months ; that the first five notes given petitioner under the first contract of December 28th, 1882, were paid at maturity, that the other five notes were partially paid at maturity and partially extended, and that the extended notes were all finally paid in full ; that of the ten notes given under the second contract of April 26th, 1883, some were partially paid at maturity and extended, and the extended notes partially paid and extended further ; and that there remains due from the Railway Company to the petitioner for steel rails the sum of \$445,175.50, with interest. The petition further states that the rails were used in the betterment of the road and were absolutely necessary, and that the indebtedness was contracted by the petitioner in consideration of the promise of the Railway Company to pay these notes out of its earnings, and that the rails were furnished with the expectation and belief that they would be paid for out of the revenue and earnings ; that the Houston and Texas Central Railway Company was placed in the hands of Receivers on or about February 1, 1885, and that when the bill was filed in this cause, April 6, 1889, to foreclose the first mortgage on the Waco and Northwestern Division, the Receivership was extended to this cause so brought for that foreclosure, and that a considerable portion of the rails was used upon the Waco and Northwestern Division. The petitioner therefore seeks to have the proportionate amount of money due for the sale of these rails paid out of the earnings in the hands of the Receiver, or, if such earn-

ings prove insufficient, then out of the proceeds of sale. But it must be especially noted that, while it appears in the petition that a large amount of the petitioner's debt has been paid, namely, the entire contract price under the first contract, and a large amount of the purchase price under the second contract, nevertheless, the petition contains no allegation to the effect that the rails which were so paid for were not the very rails which were laid on the Waco and Northwestern Division. The petitioner assumes that the Waco and Northwestern Division was relaid with rails which were not paid for, as to which there is absolutely no allegation in the petition. The allegation made in the petition (foot of page 85 of the Record) is that the petitioner is informed and believes and so avers that a large portion of the steel rails *so furnished* by petitioner to said defendant Railway Company was for the use and benefit of and was actually used upon and now constitutes a part of the railway described in the bill of complaint in this cause; but the petitioner nowhere states that those rails so furnished and used upon the railway described in the bill of complaint in this cause were not duly paid for. It is true that the Master reported that a part of the Waco and Northwestern Division was relaid with rails which were paid for, and a part with rails which were not paid for, but the petitioner makes no such allegation.

The petition further alleges that the Southern Development Company brought suit upon a similar claim in the Federal Court in Texas, being Equity Cause No. 185, and that general and special demurrers were filed to the bill, which were sustained by the Court and the bill dismissed without prejudice.

This matter was referred to a Master, who took

testimony and heard argument and finally filed a report, January 13th, 1896 (Record, page 98). In this report (which was not excepted to) the Master finds that negotiable promissory notes were given by the Houston and Texas Central Railway Company for all the rails sold under the three contracts; that all of said sales were made on a stated credit for a fixed period of time, namely, six months after the average date of each delivery, and that the defendant, the Houston and Texas Central Railway Company, had the right under the said contracts to have the time extended six months from the maturity of the notes; that said extensions were made for the accommodation and to suit the convenience of said Railway Company, and that said extended negotiable notes remaining unpaid, matured in the months of February, March, April and May, 1885; that all the rails delivered under the first contract, and about one-half of the rails delivered under the second contract, were paid for by the railway company prior to the appointment of any Receiver of its property, but that the remaining one-half under the second contract, and all rails furnished under the third contract were not paid for; that the rails furnished under the second contract were furnished under a contract made a year and ten months prior to the appointment of the Receiver in the Original Cause, No. 185, and about three years and three months prior to the appointment of the Receiver in the Consolidated Cause, No. 198, and *about six years prior to the appointment of the Receiver in Cause No. 227, in which the present intervention was filed*; that the rails furnished under the third contract were furnished under a contract made about sixteen months prior to the receivership in cause No. 185, and two years and nine months prior to the receivership in the Consolidated Cause, No. 198, and *about five years*

and six months prior to the appointment of the Receiver in Cause No. 227.

The Master also found that all of the rails had been delivered prior to the month of June, 1884, or more than eight months prior to the first receivership.

The Master further found as follows :

"I find that the debt for which the Lackawanna Company claims payment in its petition herein cannot be classed as a debt made in the ordinary course of business as its terms seem generally to be understood ; yet it appears that when the contracts hereinbefore mentioned were entered into between the said Lackawanna Company and the defendant Railway Company, the condition of the track of the defendant Railway Company was such that the demand for new rails upon the most worn portions of the roadway was practically imperative."

And further, the Master found :

"I find that when the aforesaid contracts were made with the Lackawanna Company, both seller and buyer expected the debts to be paid from the net income of the property ; that the credit extended under said contracts was at the request of and for the accommodation of the defendant Railway Company and upon its general credit ; that such sales were made without any stipulation that security should be given by the defendant company for said rails, or that payment therefor should be made out of any particular fund or in any particular way ; that said sales were for an unusually large amount of rails and the defendant was unable to pay cash therefor, and there was no way of obtaining such rails except upon a credit ; and *petitioner herein at the time of the said contracts and sales had knowledge of the mortgage of June 16, 1873, given by the defendant company upon the properties of its Waco and Northwestern division to secure the First Mortgage bonds, which said mortgage has been herein foreclosed.*"

See the Findings of the Master's Report as recited on pages 98 *et seq.*, Transcript of Record.

The Master's report was confirmed by the Circuit Court, which dismissed the petition of the intervenor. The intervenor appealed to the United States Circuit Court of Appeals which affirmed the action of the Court below.

The following **Summary of Dates** may be useful :

Main Line H. & T. C. mortgage made in 1866.

First Waco and Northwestern mortgage of the H. & T. C., June 16th, 1873.

First contract between H. & T. C. and Lackawana Iron & Coal Co., December 28th, 1882.

Second *Id.* April 26th, 1883.

Third *Id.* October 30th, 1883.

Receivers of H. & T. C. first appointed February, 1885.

Dismissed and new Receivers appointed, May, 1886.

Decree foreclosure Main Line May 4th, 1888.

Sale under decree, September 8th, 1888.

Complainants bill filed to foreclose Waco and Northwestern mortgage, and Receiver appointed, April 6th, 1889.

Decree March, 1892.

Sale to Green, December 28th, 1892.

Final sale, September 3d, 1895.

Argument.

The debt of the Lackawanna Iron and Coal Company is simply a *general contract debt* for steel rails furnished years ago by that company to the Houston and Texas Central Railway Company, at a given price per ton, for which the railway company was to give its notes, at six months, with a privilege of extension for an additional period of six months. Not a word is said in the contracts as to how the debt was to be paid, nothing about the earnings or any attempted lien thereon ; and, as the Master finds, the claim itself was in no sense to be classed with current operating expenses. But the Master

finds that the parties *expected* the debts to be paid out of the earnings. These debts were all contracted more than sixteen months before the railway company was placed in the hands of Receivers in the original cause brought by the Southern Development Company and subsequently dismissed, and nearly six years before the bill was filed in this cause to foreclose the first mortgage on the Waco and Northwestern Division, and the receivership extended thereunder. There was not a single fact connected with the transaction which gives the intervenor any lien equitable or otherwise. It is purely and simply a sale of rails to the railway company on a credit of six months with the privilege of extension for six months longer.

Before entering upon a discussion of the nature of the transaction and the general bearing upon it of the doctrine usually referred to as the doctrine of *Fosdick vs. Schall*, we submit that, even if in other respects, the petitioner could show any equities, yet these old claims upon extended notes were stale before their holder sought to enforce them. It would be obviously inequitable for Courts to recognize against property in strictness belonging to bondholders claims whose owners have not chosen to insist upon them while the railroad was still in control, but who, preferring to wait until the appointment of a Receiver, then for the first time step in relying on the hope of getting in before the bondholders in any event by virtue of such receivership. Justice Brewer, examining certain claims, for which priority was sought, in *Blair vs. St. Louis H. & K. R. Co.*, 22 Fed. Rep., 471, said :

“ Now for what time prior to the appointment of the Receiver may these credits be sustained ? There is no arbitrary time prescribed, and it should be only such reasonable time as, in the nature of things

and in the ordinary course of business, would be sufficient to have such claims settled and paid. Six months is the longest time I have noticed as yet given. Ordinarily, I think that is ample. Perhaps in some large concerns, with extensive lines of road and a complicated business a longer time might be necessary. Certainly, so far as the present road is concerned, six months is ample. If any person permits a claim to continue longer than that, he certainly has no right to be considered other than as a general creditor with no preference over a secured debt."

The petitioner must claim one of two things—either that by making this contract, it obtained a lien on the property of the railway company, entitled to preference over the then existing mortgages; or that the debt is of such a peculiar nature as to be entitled to priority of payment out of the proceeds of the sale of the railroad.

We assume that the petitioner does not claim a contract lien or mortgage paramount to the existing mortgages. It would be enough to say that the statutes of Texas as to railroad mortgages were not complied with, even if it were otherwise possible to maintain such a claim. What the petitioner claims, therefore, must be a right in equity to be paid out of the fund because it sold to the Railway Company certain rails on credit and did not collect the entire purchase-money, but took notes for it.

The right to priority of one who sells rails was settled against the intervenor as long ago as 1875 in *Meyer vs. Johnson* (53 Alabama, 237), in which the State Supreme Court said :

"Iron rails * * * when laid and fastened upon a road, are an essential part of it, and, ceasing to be chattels personal, are subjected, as a part of the road, to the older mortgages thereon," and by this Court even earlier, 1870, in the

case of the *Galveston Railroad vs. Cowdrey* (11 Wall., pp. 459, 482). There this Court held that when the creditor permitted his rails to go into and become part of the road, he consented to their being covered by the existing mortgages; that he acquired no lien which could displace such mortgages, and that a claim for priority could not be sustained. In the case at bar the situation is even stronger in favor of the mortgagee, for the Master has found specifically that the petitioner, when it furnished these rails, *knew of the mortgage upon the railroad property*.

In the case of the *United States vs. New Orleans R. R.* (12 Wall., 362), this Court affirmed the principle of the *Galveston* case, and again in *Porter vs. Pittsburg Steel Company* (122 U. S., 267).

In the case of the *Atlantic, Mississippi and Ohio R. R.* (3 Hughes, 320), the Court held that those furnishing steel rails were entitled to no priority, as was done in the case of *Olyphant vs. St. Louis Ore and Steel Co.* (28 Fed. Rep., 729).

This last case was one in which the Lackawanna Iron and Coal Company, the present petitioner, had contracts for the delivery of rails which were partially carried out, and sought, as it does now, a lien for the balance, which lien was denied and the petition dismissed.

To the same effect is *Bound vs. South Carolina Ry. Co.* (58 Fed. Rep., 473).

It is, we believe, without example or precedent that such a claim as that of the intervenor should be sustained. Such claims are mere debts, with no lien or privilege affixed to any property against which they can be enforced in a Court of Chancery.

Until the decision of *Fosdick vs. Schall* (99 U. S., 235), in 1878, and contemporary and subsequent

cases, no lawyer would ever have dreamed of going into a court of equity with such a claim.

The present petition is an experiment at a novel, unjust and unauthorized extension and perversion of the doctrine of *Fosdick vs. Schall*, and kindred cases, to go far beyond the principles of those decisions, and, in fact, to revolutionize the primary elements and most settled doctrines of equity jurisprudence and practice.

The principle of *Fosdick vs. Schall* has been discussed so frequently that any further discussion of it seems to require an apology. We may be allowed, however, to remind the Court of a few matters relevant to that case and which must, we submit, govern the issues here. *Fosdick vs. Schall* was a suit by a mortgagee, in which he applied for and obtained a Receiver, the Court imposing a condition that the Receiver should pay out of the *current earnings* all debts due and owing for labor and services rendered in operating the railroad within the next preceding three months, and all indebtedness of engines, iron, wood, supplies, cars or other property purchased within the said period of three months for the use of the company. Schall had a claim for rent of cars, and claimed priority to the mortgage out of the proceeds of the sale of the mortgaged property. The Supreme Court rejected his claim; but the Chief Justice took occasion to lay down the doctrines on which allowances could be rightfully made out of the earnings in the Receiver's hands, or out of the proceeds of the sale of the mortgaged property. This opinion was evidently delivered after great consideration, and has since been repeatedly referred to by the Court as a guiding precedent.

It will be seen from the above summary that the Court in the *Schall* case was simply applying the doctrine that the earnings of a railroad company,

even when its mortgage extends to income, are primarily applicable to the operating expenses of the company until actually sequestered by or for the mortgagee. It therefore held that under certain equitable conditions this income, even after being so sequestered, must be applied to the payment of certain limited classes of operating claims when, but for some diversion *beneficial to the mortgagee*, those claims would have been paid, as required by law, out of the earnings of the company before sequestration. As this Court, speaking through Mr. Chief Justice Fuller, said in the case of *Morgan's Company vs. Texas Central Railway Company*, (137 U. S., 171, at page 197),—

“The doctrine of *Fosdick vs. Schall* (99 U. S., 235), is that a Court of equity may make it a condition of the issue of an order for the appointment of a Receiver, that certain outstanding debts of the company shall be paid from the income that may be collected by the Receiver or from the proceeds of sale; that the property being in the hands of the Court for administration as a trust fund for payment of incumbrances, the Court, in putting it in condition for sale, may, if needed, recognize the claims of materialmen and laborers, and some few others of similar nature, accruing for a *brief period* prior to its intervention, *where current earnings have been used by the company to pay mortgage debt or improve the property, instead of to pay current expenses, under circumstances raising an equity for their restoration.*”

If any pretense be made here that any current earnings of the railroad company, properly applicable to the payment of the petitioner's claim, were used by the company to pay any part of the debt due under the mortgage on the Waco and Northwestern Division or to improve the property for the benefit of that mortgage, it must be remembered that the contracts un-

der which the petitioner's rails were furnished were all dated before November 1st, 1883, and that the original six months' notes, and the extended notes, had all matured and become enforceable by May, 1885. The first default in the payment of coupons on the bonds secured by this mortgage did not occur until the following year and more than six months after the maturity of the last of the extended notes, and when it did occur, the property was in the hands of the Receiver appointed in the foreclosure suit of the trustees of the mortgage on the main line. Clearly no diversion of income had taken place to the advantage of the Waco and Northwestern Division mortgage and in detriment to the rights of the petitioners.

It is true that the Railroad Company paid some interest on its mortgages, including the Waco and Northwestern Division mortgage, after these contracts had been made.

But it cannot be claimed that the bondholders, whose interest was so paid by the railroad company, were bound to take notice that the railroad company had incurred a large debt for rails which it had not paid. In the case of *Morgan's Company vs. Texas Central Railway Company* (137 U. S., 171), an attempt was made to assert a preference for money loaned because it was used for the payment of coupon interest, but this Court affirmed the action of the Court below in ruling out any such claims.

Nothing could be more certain than that the Court in *Fosdick vs. Schall* laid down no doctrine from which it could be justly argued that the current-fund creditor has any *lien* upon the *earnings* or the *corpus* of the property. No one could have said more plainly than the Chief Justice, if such

had been his intention, that the current-earnings creditor has a prior lien to the mortgage creditor, and is entitled for its enforcement to the same remedy in equity that the mortgage creditor possesses for his lien. If such had been the principle of the opinion, so carefully matured and expressed, it would have been made clear. Instead of this, the right of the current-earnings creditor is most carefully subjected to that "sound judicial discretion, which may, under the circumstances of the particular case, appear to be reasonable."

The case of *Express Company vs. Railroad Company*, (99 U. S., 191), decided at the same term as *Fosdick vs. Schall*, throws the strongest light on this branch of the case. The Express Company advanced \$20,000 to the railroad company to be expended in repairing and equipping its railroad, for which it was to have certain express facilities, accounts to be made monthly, and to continue for a year, and until payment of the \$20,000. The railroad company then executed a deed of trust to secure mortgage bonds, a foreclosure suit was brought and a Receiver appointed. The Receiver refused to complete the contract, and the Express Company sued in equity for its performance, which, of course, involved compensation therefor. Mr. Justice SWAYNE said, at page 200:

"The appellant has no lien. * * * As well might he (the Receiver) be decreed to satisfy the appellant's demand by money as by the service sought to be enforced. Both belong to the lien-holders and neither can be thus diverted. The appellant can therefore have no *locus standi* in a Court of equity."

Judge DRUMMOND, the father of railroad foreclosures, in *Turner vs. Railway Company*, (8 Biss., 315,) said :

“ During the discussions which have taken place on this subject, the allowance of these back claims has been sometimes called a lien, but in point of fact it never has been nor can it be justly so called, but, as already stated, is an exercise of the equitable power of the Court in the premises.”

Milttenberger vs. Railroad, (106 U. S., 286,) decided in 1882 by Justice Blatchford, was a case where default on the first mortgage occurred in November, 1873, on the second mortgage in January, 1874, and suit for foreclosure was brought by the mortgagee in August, 1874. A Receiver was appointed, with directions to pay the arrears due for operating expenses incurred within ninety days, and to pay not exceeding ten thousand dollars to competing lines and for materials and for repairs and ticket and freight balances ; also to make certain improvements and purchases, and this was sustained. This Court said in the course of its opinion, page 311 :

“ It can not be affirmed that no items which accrued before the appointment of a Receiver can be allowed in any case. Many circumstances may exist which may make it necessary and indispensable to the business of the road and the preservation of the property for the Receiver to pay pre-existing debts of certain classes out of the earnings of the Receivership, or even the *corpus* of the property, under the order of the Court, with a priority of lien. Yet the discretion to do so should be exercised with very great care. The payment of such debts stands *prima facie* on a different basis from the payment of claims arising under the Receivership, while it may be brought within the principle of the latter by *special circumstances*. It is easy to see that the payment of unpaid debts for *operating* expenses, accrued within the *ninety* days, due by a railroad company suddenly deprived of the control of its property, due to operatives in its employ, whose cessation from work simultaneously is to be deprecated in the interests both of the property and of the public, and the payment of limited amounts due to other and con-

necting lines of road for materials and repairs, for unpaid ticket and freight balances, the outcome of indispensable business relations, where a stoppage of the continuance of such business relations would be a probable result in case of non-payment, the general consequence, involving largely also the interests and accommodations of travel and traffic, may well place such payments in the category of payments to preserve the mortgaged property in a large sense by maintaining the good will and integrity of the enterprise, and entitle them to be made a first lien."

It is clear that no idea was in the mind of the Court that those claims or any of them, prior to the Receivership, were liens upon the property. They were claims limited by the Court's description to certain peculiar classes of operating expenses, the payment of which might almost be regarded as a necessity for the preservation of the property. The Receiver had put the payment of this class of claims on the ground that "it was indispensable to the business of the road, and unless authorized to provide for them at once, the business of the road would suffer great detriment. These reasons were satisfactory to the Court." Such claims are widely different from those of a steel company which, knowing of the existence of the mortgage, and relying on the earnings of the road, chose to supply steel rails to the railroad company long before any default on the bonds or the appointment of a Receiver. The remarks of the Court, in the *Miltenberger* case, even if given their widest scope, would apply only to those simple, current debts arising necessarily in the daily business of the railroad, the failure to pay which would result in the practical cessation of that business. It is not merely because the materials furnished by the holders of claims are useful to the road, or because the claimants might refuse to do

business in future with the railroad company, that priorities will be allowed over the mortgage debt. It is to be presumed that railroad companies do not buy things which seem useless for their purposes ; and some of the claims in the *Milltenberger* case were expressly disallowed, although "the creditors threatened not to furnish any more supplies on credit unless they were paid the arrears." The most careful discrimination must be exercised in every case, and no disbursement authorized with priority unless some *special* equities appear surrounding that specific claim. What constitutes such special equities, even after the numerous decisions of this Court and other Courts on the subject, still remains somewhat vague ; and we respectfully submit that a close review of the authorities will disclose that in every well-considered decision the elements of *consent* or *estoppel on the part of bondholders* will be found to exist, as they undoubtedly existed in the *Milltenberger* case. But, in any event, the Court can find no special equities, in the absence of consent, in favor of claimants such as the present petitioner.

The case of *Trust Company vs. Souther*, (107 U. S., 591), arose where default had been made in the payment of mortgage interest due October 1st, 1873, and semi-annually thereafter. On December 6th, 1879, the mortgagee filed a bill of foreclosure and obtained a Receiver, the order appointing him requiring the Receiver to pay and discharge all amounts due and owing for labor or supplies accrued in the operation and maintenance of the road within six months immediately preceding. The net earnings of the receivership exceeded \$200,000, which, *with the assent of the mortgagee*, were expended in purchasing additional land and rolling-stock and making permanent improvements of the railroad, all of

which were embraced in the sale, leaving about \$65,000 of debts unpaid, of the character which the Receiver had been ordered to pay. The question was as to their right to payment out of the proceeds of sale. The Chief Justice said that their right to such payment was decided by *Fosdick vs. Schall* and *Miltenberger vs. Railroad Company*, and held that, as the net earnings, instead of being applied to pay the current operating debts as directed, *had been diverted at the request of the mortgagee, to add to the value of the mortgaged property*, the proceeds of sale would, in equity, be held to represent the fund directed to be applied to the labor and supply creditors when the Receiver was appointed.

In *Burnham vs. Bowen*, (111 U. S., 776), a mortgage had been executed in June, 1871, to secure bonds for \$4,125,000. No interest was ever paid, the company remaining in possession and operating the road until 1875, when a suit for foreclosure was commenced and a Receiver was appointed. The receivership earned over \$25,000 of net earnings. All those net earnings, together with the railroad, went into the hands of the mortgagee, by strict foreclosure, but subject to the claim of Bowen, amounting to \$6,515.42 for coal sold to the railroad company in 1874—"one of the current debts for operating expenses, made in the ordinary course of a continuing business, to be paid out of the current earnings," and there was no other liability on account of current expenses unprovided for when the Receiver took possession. This claim would have been paid out of current earnings, at maturity, had the Court not interfered, at the instance of the trustees, for the protection of the mortgage creditors.

Out of his earnings the Receiver had paid \$7,898, a debt for real estate for the company, and nearly

\$18,000 for right of way. The Court held that the right of Bowen for payment out of the earnings by the Receiver, was within the principle of *Fosdick vs. Schall*, those earnings having been diverted to payment for additional property to increase the security of the mortgage debt. But the opinion declares, at page 783 :

“ We do not now hold any more than we did in *Fosdick vs. Schall*, or *Huidekoper vs. Locomotive Works*, (99 U. S., 258, 260), that the income of a railroad, in the hands of a Receiver for the benefit of mortgage creditors, who have a lien upon it under their mortgage, can be taken away from them and used to pay the general creditors of the road.”

In *Blair vs. Railway Company*, (22 Fed. Rep., 471, already cited in another connection, Justice BREWER said, at page 474 :

“ What claims are entitled to such equitable preference? The Master has reported in favor of all claims accruing since the default in payment of the interest on the mortgage debt—a period of over two years. This seems to proceed upon the assumption that the mortgagees, by failing to take action, have made the mortgagor company their agent to incur debts—have impliedly consented that all such debts shall take preference of their secured claims. I do not think that this principle is sound. There is no implied agency to that extent, and I do not think that the rulings of the Supreme Court are based upon any such doctrine. The idea which underlies them I take to be this : That the management of a large business like that of a railroad company cannot be conducted on a cash basis. Temporary credit in the nature of things is indispensable. Its employees cannot be paid every month. It cannot settle with other roads its traffic balances at the close of every day. Time to adjust and settle these various matters is indispensable. Because in the nature of things this is so such temporary credits must be taken as assented to by the mortgagees, because both the mortgagees and the public are interested in keeping up the road and having it pre-

served as a going concern; and whatever is necessary to accomplish this result must be taken as assented to by the mortgagees. In this view, such temporary credits accruing prior to the appointment of the Receiver must be recognized by the mortgagees and such claims preferred." * * *

* * * "Out of what shall these claims be paid? Primarily, of course, out of the earnings of the road, and ordinarily out of such earnings alone. * * * That is fair, because if no receiver were appointed and the claimants attempted by legal process to enforce the collection of their claims they could obtain no priority over the mortgages, but must still be subject to such mortgages. So the appointment of a receiver ought not to give them a priority which they had not before."

Justice Brewer then went on to say that cases may arise in which such claims may be paid even out of the *corpus* of the property, but this is only in exceptional cases, and where *special* equity is shown.

The claim of the present intervenor contains no such special equity, and is not of a character which under a receivership obtained by the mortgagee would entitle it to an equitable preference against either the *earnings* or the *corpus*.

In *Bound vs. South Carolina Railway Co.* (58 Fed. Rep., 473,) which was an application by this very petitioner, almost identical with the present application, the Circuit Court of Appeals for the Fourth Circuit, consisting of Chief Justice FULLER and District Judges HUGHES and MORRIS, denied the priority prayed for, using in the course of their opinion the following language, at page 480:

"The rule giving preference to current expenses incurred on the faith of the earnings of a railroad shortly before the appointment of a Receiver has never been carried so far. The debt of the Lackawana Company was an ordinary merchandise debt, evidenced by notes, which were re-

newed from time to time. * * * The Railroad property being heavily mortgaged, all that any unsecured creditors had to look to for payment was the earnings. The immediate earnings, it is clear, the Lackawana Company did not look to, as the sale was upon a credit of eight months. * * * The claim is quite different from those ordinary and necessary current expenses of operating a railroad contracted but a short time before a receivership, and which, by the sudden action of the court in appointing a Receiver are left unpaid."

The effort to bring within the scope of the doctrine of *Fosdick vs. Schall*, all manner of general debts of railroad companies has been severely discountenanced by this Court. In the case of *Kneeland vs. Trust Company* (136 U. S., 89), it said at page 97 :

"No one is bound to sell to a railroad company or to work for it, and whoever has dealings with a company whose property is mortgaged must be assumed to have dealt with it on the faith of its personal responsibility and not in expectation of subsequently displacing the priority of the mortgage liens. It is the exception and not the rule that such priority of liens can be displaced. We emphasize this *fact of the sacredness of contract liens for the reason that there seems to be growing an idea that the Chancellor, in the exercise of his equitable powers, has unlimited discretion in this matter of the displacement of vested liens.*"

We have quoted from these few leading authorities because they illustrate the real meaning of the rule. We will do no more than refer the Court to some of its many other decisions on this subject, from which, we submit, it clearly appears that the petitioners' claim is not entitled to priority over the bondholders. *Hale vs. Frost* (99 U. S., 389); *Huidekoper vs. Locomotive Works* (99 U. S., 258); *Union Trust Co. vs. Walker*, (107 U. S., 596); *Union Trust Co. vs. Illinois Midland R. R. Co.* (117 U. S., 434); *Porter vs. Pittsburg Bessemer Steel Co.*

(120 U. S., 649); *Penn vs. Calhoun* (121 U. S., 251); *Porter vs. Pittsburg Steel Co.* (122 U. S., 267); *Union Trust Co. vs. Morrison* (125 U. S., 591); *St. Louis, Alton & Terre Haute R. R. Co. vs. Cleveland R'y. Co.* (125 U. S., 658); *Wood vs. Guarantee Trust Co.* (128 U. S., 416); *Thompson vs. Water Valley R. R. Co.* (132 U. S., 68); *Fogg vs. Blair* (133 U. S., 534); *Toledo, Delphos & Burlington R. R. Co. vs. Hamilton* (134 U. S., 296); *Louisville, Eansville & St. Louis R. R. Co. vs. Wilson* (138 U. S., 501); *Sunflower Oil Co. vs. Wilson* (142 U. S., 313); *Quincy R. R. Co. vs. Humphreys* (145 U. S., 82); *St. Joseph R. R. Co. vs. Humphreys* (145 U. S., 105); *United States Trust Co. vs. Wabash Western R'y Co.* (150 U. S., 287); *Thomas vs. Western Car Co.* (149 U. S., 95).

These authorities confine the *class* of claims to which priority will be given with great strictness to those expenses which, being operating expenses of a daily character, form part of the necessary current cost of running the road and without which the road could not continue as a going concern. The class does not extend to any other claims, however useful in character or necessary to the general welfare of the road. Original construction claims, for instance, as to the equity of which certainly as much might be said as of the present intervention, are uniformly held to fall outside of the rule. See *Wood vs. Guaranty Co.*, *supra*.

But even in the case of claims falling within the recognized class, the earnings of a Receivership cannot be taken away from the mortgagee and given to the unsecured claimant, unless the latter can point to some *diversion* to the use of the mortgagee of earnings, which, in justice, belong to him. To make earnings belong in justice to the current earnings creditor, they must obviously be the cur-

rent earnings of the *Railroad Company* (the sole party who incurred the debt) applicable to the payment of current expenses and earned at the time when the debt was *incurred* or when, in the ordinary course of business, it *matured*. Specifically applying these obvious rules to the case at bar, even if the petitioner's claim were of the class to which Courts have awarded priority (which, as the master found, it is not), the petitioner would still have to show that current earnings of the *Railroad Company*, earned at the time when the debts for the steel rails were *incurred*, or when they, in the ordinary course of business, *matured*, had been actually taken and applied to the benefit of the holders of the bonds secured by the Waco Division mortgage. This, plainly, the petitioner cannot do. If any specific earnings could be considered primarily applicable to the payment of the petitioner's claim, they could only in justice be those earnings of the *Railroad Company* earned at the time (a), when the contracts were made, (b), when the rails were delivered, or (c), when the notes matured.

We understand the petitioner to claim that *during the receivership* certain moneys were paid to the bondholders of the Waco and Northwestern Division for interest on their bonds, which moneys should have been paid on account of the petitioner's debt, and that therefore it is entitled to have at least that amount refunded out of the proceeds of sale. But this begs the entire question. The mortgage creditors are entitled to sequester the income, and they have a right to have such income paid over to them, or applied on the property for their benefit, after the Receiver has paid out of the income the regular operating expenses, and such unpaid bills for operating expenses, etc., as are en-

titled to preference. The fact that the intervenor is a creditor does not give its claim a preference for payment out of the income over the bondholders, who are also creditors, and for whose benefit the income as well as the corpus of the property was especially pledged. The fact that the Railroad Company contracted a debt years before the receivership was begun for the purchase of rails, and used the rails for the improvement of its railroad, does not give that simple contract debt preference over the secured mortgage debt or change its character, so that the unsecured creditor can seize the income or ask that the property be charged with a prior lien for its benefit, because the secured creditor has received some of his interest debt.

It is absolutely essential for the petitioner in the first instance to show that its claim has priority, and that it is such a claim as the Courts recognize as entitled to payment before the payment of the mortgage debt. We have shown that such is not the case; that it never had such right to prior payment, and that if it ever could have asserted such a right the time for its doing so expired long ago. The latest of the petitioner's contracts was made nearly two years before the original receivership in 1885 in the Southern Development case, which was dismissed.

The petitioner's counsel will perhaps seek to draw an argument from the fact that the trustee of the Waco Division mortgage did not file a bill to foreclose that mortgage immediately upon default. But it must not be forgotten that the first default on the Waco Division mortgage did not occur until January, 1886, long after the property had been placed in the hands of a Receiver by another party, and long after the last of

the petitioner's extended notes had matured. Thus the petitioner's claim had arisen, ripened and grown old, before the trustee came into a position to act. How, then, can the petitioner base any equities on the failure of the trustee to begin foreclosure immediately? Its rights having all accrued prior to the default, what effect upon them could the future course of the trustee possibly have? The delay of bondholders to act upon a default cannot of itself create any rights in others. It may, undoubtedly, under some conditions, form an element in a situation which would make it inequitable for delaying bondholders to insist upon their mortgage priority. But such a consequence can plainly not flow from delay where, as here, the claim of the adverse petitioner had become complete, mature and enforceable before the delay began. The rights of the petitioner were preserved by its successive intervening petitions in the three causes, but they were necessarily preserved in their *original* condition. They could not improve by the mere lapse of time, nor could the clauses in the several orders and decrees relating thereto in any way change the relations of the parties. Thus, the whole controversy is relegated back to the original question, which is whether the petitioner had acquired any equity against the Waco and Northwestern Division bondholders at the beginning of the Receivership. As we have already shown that question must be answered in the negative.

As illustrating the part played by delay of bondholders in such proceedings, we call the Court's attention to the cases of *Boom Co. vs. Case*, (4 Fed. Rep., 873); *Blair vs. St. Louis H. & K. Co.* (22 Fed. Rep., 471); *Farmers' Loan and Trust Company vs. Green Bay, W. & St. P. Ry. Co.* (45 Fed. Rep., 664), and *Coe vs. New Jersey*

Midland Ry. Co. (31 N. J. Eq., 105). All of these cases were decided on the obvious principles summarized above.

"It has never been decided yet," as the Court said in *The Atlantic, Mississippi and Ohio Case*, (3 Hughes, 340), "that because a mortgagee does not immediately pounce upon his security, foreclose, take possession and sell, that he impairs the obligation of his lien."

The decrees of the Circuit Court and the Circuit Court of Appeals dismissing the intervenor's petition should be affirmed.

New York, January, 1898.

HERBERT B. TURNER,

M. F. MOTT,

Solicitors and of Counsel for the
Farmers' Loan and Trust Company.

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM 1898.

No. 162

LACKAWANNA IRON AND COAL COMPANY, ET AL.

APPELLANTS.

VS.

FARMERS' LOAN AND TRUST COMPANY, ET AL.

APPELLEES.

BRIEF FOR APPELLEES MORAN BROS. AND

HENRY K. MCHARG.

The subject of appellant's intervention in the Circuit Court was the sale and delivery by the Lackawanna Iron and Coal Company to the Houston and Texas Central Railway Company, prior to the appointment of a receiver over the property of said company, and during the years 1882 and 1883, of 18,581 tons of steel rail at an aggregate agreed price of \$735,454.30.

The object sought by intervenors in this proceeding is to obtain priority in the payment of their claim over the mortgage bond-holders out of the proceeds of the sale of the property, or the net income arising from the operation of the road. The claim was referred to a special master who was ordered to hear the evidence and report the facts to the Court. The complainant and these appellees intervening bond-holders appeared before the master and after pleading the general issue, specially pleaded that the claim was stale and barred by laches and barred by the Texas Statue of four years limitation. The master in due time filed his report, which was not excepted to and is copied in full in the record. Upon the hearing a decree was entered confirming the report and dismissing the petition. From the decree of the Circuit Court appellants appealed to the Circuit Court of Ap-

peals and the decree of the lower Court was by that Court affirmed for the reasons set forth in its opinion copied in the record, pages 130 to 140 and the case is here on certiorari, granted by this Court.

First Proposition.

Before a debt contracted by a Railway Company prior to the appointment of a receiver will be given priority over the debt of the bond-holders secured by a prior mortgage on the road, it must appear in cases where the debt is for supplies or material, (1) that it is the purchase price of current supplies needed from time to time to keep the road in repair, (2) bought on temporary credit, which credit resulted from the nature and character of railroad business, (3) that such purchase was made within a reasonable time prior to the appointment of a receiver of the property.

STATEMENT.

1. The master finds: "I find that the debt for which the Lackawanna Claims payment in its petition, *cannot be classed as a current debt*, made in the ordinary course of business; * * * that the credit extended under said contracts was at the request of and for the accommodation of the defendant Railway Company, and upon its general credit, * * * without any stipulation that security should be given by the defendant company for said rails, or that payment therefor should be made out of any particular fund or in any particular way; that said sale was for an *unusually large amount of rails*, and defendant was unable to pay cash therefor." (R. p. 104.) The magnitude of these dealings becomes apparent upon an examination of the master's findings. In the period of about fourteen months defendant bought of the Lackawanna Company 18,581 tons of rail, at an aggregate cost of \$735,454.30, which at 88 and 84.86 tons per mile for 56 and 54 pound rails respectively, were sufficient to construct anew 214.77 miles of track. (R. p. 98 to 104.)

2. The master further finds: "I find that negotiable promissory notes were given petitioner by the defendant company for all rails sold under the three contracts; *that all of said sales were made on a stated credit for a fixed period of time, viz: six months after the average date of each delivery*, and that said defendant company had the right, under said contracts, to extend the time six months longer from the maturity of said notes; that such extensions were made for the accommodation and to suit the convenience of said defendant company and that said extended negotiable notes remaining unpaid matured as shown in clauses 2 and 3, during the months of February, March, April and May, 1885." (R. p. 103.) The above finding shows that the credit was voluntarily extended, and did not result from the nature of the business or necessities of the case.

3. The sales were not made within a reasonable time prior to the appointment of a receiver over the property. On this subject the master finds:

"I find that all the rails delivered under the first contract, and about one half of the rails delivered under the second contract were paid for by the Railway Company prior to the appointment of any receiver of said property, but that the remaining half under the second contract, and all rails furnished under the third contract, are not paid for.

"I find that the rails furnished under the *second contract* were furnished under a contract made *a year and ten months prior* to the appointment of the receiver in cause No. 185, and about *three years and three months prior* to the appointment of a receiver in Consolidated Cause No. 198, and about *six years prior* to the appointment of the receiver in *this cause*.

"I find that the rails furnished under the *third contract* were furnished under a contract made about *sixteen months prior* to the receivership in cause No. 185, and about *two years and nine months prior* to the receivership in Consolidated Cause No. 198, and about *five years and six months prior* to the appointment of a receiver in *this cause*." R. p. 103.) (*Italic ours*.)

This report was not excepted to by any one and at the hearing of the case in the Circuit Court was in all things confirmed (R. p. 121-2.) but the testimony heard by the Master and the Circuit Court was not brought up and is not in the record. The report of the Master was substantially adopted by the Circuit Court of Appeals in the following language: (*Italics ours*.)

"The case of *Burnham vs. Bowen*, *supra*, relied on by the intervenor's counsel and claimed to be analogous in principle to the instant case, was based on a demand for coal used in running the locomotives, supplied to the railroad company a few months before the appointment of a receiver, and the claim was found by the Supreme Court to be, "One of the current debts for operating expenses made in the ordinary course of continuing business." We discover no similarity of principle between that case and the case at bar, Coal is an article of constant and uninterrupted consumption on a railroad, and its purchase at short intervals, for the purpose running the locomotives in quantities not exceeding the operating requirements of the road are clearly current expenses of the road. But it is difficult to see how the purchase of 20,000 tons of rails made under the circumstances stated in the intervenor's own pleadings can be a current debt, "for operating expenses made in the ordinary course of continuing business." *If the road was in the condition of delapidation, which is inferable from the intervenor's averments, it might be sufficient to say, in denying the demand that the rails were supplied, not as a matter arising in the ordinary course of a railroad's operations, but for the virtual reconstruction of the road.* No authorities need be cited to establish the prop-

osition that works of reconstruction are not entitled to preferential payment."

And further on the court say:

"The unusually large purchase of rails; the time within which they were to be delivered, the condition of the road, the contracts providing for notes at six months renewable for a like term at the maker's option, the hypothecation of securities for the payment of the claim, the knowledge which the intervenor had of the mortgage, the fact that the contracts contained no promise to pay out of any particular fund, the time which elapsed between the date of the contracts and the appointment of a receiver in cause No. 185— are circumstances, which taken together cannot fail to convince us that the *intervenor relied upon the general credit of the railway company.*" R. p. 134 and 140.

This court in the case of *Stewart vs. Hayden*, 169 U. S. p. 1; 18th Supreme court Rep., page 274, uses this language, "We will add that, as the circuit court and the circuit court of appeals agreed as to what were the ultimate facts established by the evidence, this court should accept their view as to the facts, unless it clearly appeared that they erred as to the effect of the evidence. *Morewood v. Enegquist*, 23 How. 391. *The Ship Marcellus*, 1 Black, 414, 417; *Dravo v. Fabel*, 132 U. S. 487, 490, 10 Sup. Ct. 170; *Companio De Navigation La Flecha vs. Brauer*, 168 U. S. 104, 123, 18 Sup. Ct. 12." See also *The Carib Prince*, 170 U. S. 645, 18 Sup. Ct. Rep. 753. We assume from the foregoing that this court will not review the findings of fact thus concurred in by both the Circuit Court and the Circuit Court of Appeals. But if this court were disposed to go into the evidence, we call attention to the fact that no exceptions were taken to the master's report and that no evidence is brought up in the record. Appellants have therefore deprived this court of the opportunity of examining the evidence. The facts being established that the claim cannot be classed as a current debt, that the rail was sold upon the general credit of the Railway Company, and in unusually large quantities, and for virtually reconstructing the road, we invite the court's attention to the law as announced in a few of the leading opinions of this court arising out of a similar state of facts.

The case of *Fosdick vs. Schall* 99 U. S. 235 is cited and relied on by appellant's counsel and by us. The principles settled by that case are familiar to this court and control this one and fully support the opinion of the Circuit Court of Appeals in this case. That was a case where priority was claimed by a creditor for rent of certain cars sold to the Railway Company prior to the appointment of the receiver. The priority was denied by this Court and in concluding the opinion, the court used this language: (*Italics ours.*)

"There is nothing to show that the current income of the receivership or of the Company has been in any manner employed so as to deprive this creditor of any of his equitable

rights. In short, as the case stands, no equitable claim whatever has been established upon the fund in court. *Prima facie* that fund belongs to the mortgaged creditors, and the presumption which thus arises has not been overcome. Schall, for the balance, his due, after his own security has been exhausted, occupies the position of a *general creditor* only."

In the case of *Huidekoper vs. Locomotive works*, 99 U. S. 258, decided at the same time the distinction between a general debt of the company and debts for current or other expenses is made very clear, and having applied that distinction in the latter case, this court denied the claim for priority in this language, (*italics ours*.) "We think the case is settled by that of *Fosdick v. Schall*, *supra*. p. 235. The amount found due the locomotive company *is not in reality for the use and repairs of the engines, but on account of what was agreed to be paid for the purchase*. The railroad company contracted to buy the engines and pay a certain price. The locomotive company retained a paramount lien to secure the sum to be paid. The debt so incurred was not paid. The lien of the locomotive company has been in effect foreclosed, and the balance of the debt still remains due. Whatever may have been the form of the transaction, this is its substance. So far as we can see, *no equitable claim upon any fund in court has been established as security for this debt*. The locomotive company occupies the position as *general creditor with no special equities in its favor*."

The case of *Burnham vs. Bowen*, 111 U. S. p. 776, is relied on by counsel for appellants as supporting their claims to priority. We call attention to the language of Chief Justice Waite showing that the claim allowed in that case was for current expenses, etc. In delivering the opinion of the court, among other things he said (*italics ours*), "In the agreed facts, upon which the case was heard below, it is stated that the coal was furnished during the year 1874, but the precise time in the year is not given. From what does appear however, *we are satisfied that, at the time of the appointment of the receiver, this was one of the current debts for operating expenses made in the ordinary course of a continuing business, to be paid out of current earnings, and that the payment would have been made at the time agreed on if the Company had remained in possession*." And further he said: "In the present case, as we have seen, *the debt of Bowen was for current expenses and payable out of current earnings*." The foregoing extracts from the opinion clearly show that the case turned on the fact that the claim was for current expenses and of course that case is not authority for this one.

The case of *Hale vs Frost* 99 U. S. 391 is also cited by counsel as supporting their claim to priority. The opinion in that case is short but the distinction is again recognized between claims for current expenses and material for construction purposes and as an authority it is destructive of appellants' claim for priority. In that case there were two appellants, the Union Car-spring Manufacturing Company and Hale, Ayer & Co., and

both intervened in the receivership and claimed priority over the mortgage bondholders. The Union Car-Spring Manufacturing Co's. claim was for car springs and spirals, amounting to \$469.42, which the receiver after his appointment continued to use, but had not paid for. The claim of Hale, Ayer & Co. was for the total of \$21,738.92, of which amount \$5,919.25 was for supplies, for the machinery department; \$14,944.24 for material for construction purposes, and \$875.43 interest. The court in passing these claims say, "The Union Car-Spring Manufacturing Company is entitled to payment in full, and Hale, Ayer & Co. to payment of so much of their claim only as is for supplies to the machinery department. There is nothing in the case to show any special equities in their favor in respect to that part of their account which is for *material for construction purposes.*" Thus it will be seen that the Union Car-Spring Manufacturing Company was allowed in full the whole of their claim, because the claim was for current expenses used in the operation of the road. That portion of the claim of Hale, Ayer & Co. which was for supplies to the machinery department, and which of course was for necessary expenses of the road, was allowed its priority, but that portion of the claim which was for construction purposes was disallowed. Enough has been said to show that the cases cited by appellants do not support the contention that a claim such as the facts show theirs to be has ever been given priority, and we assert that no case can be found which will support the claim to priority here asserted so long as the facts found by the lower courts are not upset and a new set of facts put in their place. These facts put appellants' case at war with every case where priority has been decreed. But appellants contend that the findings of the master that when contracts were made for the purchase of the rail that the track of the defendant Company was such that the demand for rails on the most worn portion was imperative; that the condition of the road was bad; that there was continuous breakage of rail and wrecking of trains; that the track was unsafe; that damage to merchandise, rolling stock, etc., was continuous, and that the need for new rail seemed to have been absolutely necessary as a preservation for human life, the loss of which was liable to occur at any moment, brings their case within the doctrine allowing priority. These facts prove too much, and show that the view taken of this purchase of rail by the Circuit Court of Appeals is correct that it was for virtually reconstructing the road. The master found that the sale was of an unusually large amount of rail upon the general credit of the railway company, and that the claim could not be classed as a current debt. Attention is again called to the fact that 20,000 tons of rail were contracted for in about fourteen months, and that 18,581 tons of rail were actually delivered under the contracts at the price of \$735,459.30, sufficient in amount to lay down 214.77-100 miles of new track on the road of a railway company which owned only about 500 miles of road. The court's attention is also called to the fact that these intervenors in setting out their claim describe the quantity of rail used by the

mile and the claim is in the same manner reported by the Master by the mile, R. p. 104, and this method of describing the claim of these interveners is constantly used by the solicitors for appellants in their brief, page 7. It appears that the track as it existed when this rail was purchased was taken up bodily, and a new track laid down with these rails, which makes a clear case of purchase and use for general construction purposes. R. p. 104. In *Thomas vs. Western Car Company* 149 U. S. 95, this court say, "The case of a corporation for the manufacture and sale of cars, dealing with a railroad company, whose road is subject to a mortgage securing outstanding bonds, is very different from that of workmen and employes, or of those who furnish from day to day, supplies necessary for the maintenance of the railroad. Such a company must be regarded as contracting upon the responsibility of the railroad company, and not in reliance upon the interposition of a court of equity." In the latter portion of the opinion this court again took occasion to recognize the distinction between claims for repairs and claims for construction. The court say, "Assuming, then, that the proportion of the amount shown to have been expended in the renewal of these cars was \$80.00 per car, and the rest in ordinary repairs of the kind contemplated by the contract, and deducting from the claims as made for the entire number of cars, to wit, \$19,695, the estimated cost of reconstruction, as certified to by Huideköper, \$13,920, there remains the sum of \$5,775, representing ordinary repairs, and to that extent we approve the decree of the court below in allowing for repairs."

The contention that the claim is entitled to priority on account of the claimed urgent and pressing necessity for the rail about the time the contracts were made was fully met and overcome in the opinion of the Circuit Court of Appeals. That Court said:

"That the necessity for supplies does not entitle to preferential payment unless the supplies are for current expenses in the ordinary course of operation, it is forcibly shown by the case of *Morgan's L. & T. R'y. Co. vs. Texas Central R'y. Co.*, 137 U. S., 171, in which it was substantially held that the mere fact that money was loaned to a railroad company to pay the interest on its first mortgage bonds, does not entitle the lender to preference, and that although advances of money may have enabled a railway company to maintain itself, that fact alone does not entitle the lender to priority. The contention that the intervenor is entitled to preference, because the rails supplied to it must have enhanced the value of the bondholders' security is clearly untenable. In *Railway Co. vs. Cowdry*, 11 Wall, 482, Mr. Justice Bradley, as the organ of the court, said:

"As to the point of giving priority to the last creditor for aiding to conserve the thing, all that is necessary to say is, that the rule referred to has never been introduced into our laws except in maritime cases which stand on a particular reason." Also see *Thomson vs. White Water Valley R. R.*, 132 U. S. 68;

Jones on Corporate Bonds and Mortgages, sec. 584; *Fogg vs. Blair*, 133 U. S. 534; *Toledo R. R. Co. vs. Hamilton*, 134 U. S. 296.

The claim asserted in last case was the price agreed to be paid to Thomas Hamilton, a contractor, who intervened and showed that under three several contracts with the Railroad Company, he constructed a dock on the Maumee River, in the City of Toledo. The lot on which the dock was built was a part of the railroad property covered by the first mortgage given by the Company. The Circuit Court sustained the claim of Hamilton and decreed prior payment on the amount due him out of the proceeds of the sale of the railroad property, and based the right of recovery on the ground of superior equity. Mr. Justice Brewer in delivering the opinion of the court says:

"We think that the views of neither the master nor the court can be sustained, and that it was error to give appellee priority over the mortgage. It will be noticed, and it is a fact which lies at the foundation of this case, that the contracts for the construction of the dock was not made till more than three years after the execution and the record of the mortgage. The record imparted notice to Hamilton and to all others, of the fact and terms of the mortgage; and the question is thus presented, whether a railroad company, mortgagor, can, three years after creating by recorded mortgage an express lien upon its property, by contract with a third party displace the priority of the mortgage lien. It would seem that the question admits of but a single answer. Certainly, as to ordinary real estate, no one would have the hardihood to contend that it could be done, and there is in this respect no difference between ordinary real estate and railroad property. A recorded mortgage, given by a railroad company on its road-bed and other property, creates a lien whose priority cannot be displaced thereafter, directly by a mortgage given by the Company, nor indirectly by a contract between the Company and a third party for the erection of buildings or other works of original construction," and further on he says:

"Neither did the fact of the construction of the dock and the subsequent improvement of the mortgaged property, give, as reported by the Master, to Hamilton, an equitable lien prior in right to the lien of the mortgage, or furnish equitable reasons why the legal priority belonging to the mortgage should be displaced. It is true, cases have arisen in which, upon equitable reasons, the priority of a mortgage debt has been displaced in favor of even unsecured subsequent creditors. See *St. Louis, etc., R. Co. vs. Cleveland, etc. R. Co.*, 125 U. S. 658, 8 Sup. Ct. Rep. 1011, in which many of these cases are collected, and the equitable principles underlying them stated. But those principles have no application here. The work which

Hamilton did was in original construction, and not in keeping up, as a going concern, a railroad already built. The amount due him was no part of the current expenses of operating the road."

In *Morgan's Louisiana & Texas Railroad & Steamship Co. vs. Texas Central Railroad Company*, 137 U. S., p. 171; 11th Supreme Court Reporter, page 69 this court says:

"To allow another corporation, which for its own purposes has kept a railroad in operation in the hands of the original company by enabling it to prevent those who would otherwise be entitled to take it from doing so, a preference in reimbursement over the latter on the ground of superiority of equity, would be to permit the speculative action of third parties to defeat contract obligations, and to concede a power over the property of others which even governmental sovereignty cannot exercise without limitation. And if all these advances should be considered as applied in payment of the operating expenses only, upon the theory, where such was not literally the fact, that they supplied a deficit created by the payment of interest out of the gross earnings, the same remarks would be applicable."

Counsel for appellants cite *Miltenberger vs. Loganport C. & S. W. R. Co.*, 106 U. S., 285, 1 Sup. Court Reporter, 140. Examination of the opinion delivered in that case shows that it decides nothing new but is in harmony with the other decisions of this court. The opinion in that case was ~~given~~^{delivered} by Mr. Justice Blachsford, and among other things he says; (Italics ours.) "Many circumstances may exist which may make it necessary and indispensable to the business of the road and the preservation of the property, for the receiver to pay pre-existing debts of certain classes out of the earnings of the receivership, or even the *corpus* of the property, under the order of the court, with a priority lien. Yet the discretion to do so should be exercised with very great care. The payment of such debts stands *prima facie*, on a different basis from the payment of claims arising under the receivership, while it may be brought within the principle of the latter by special circumstances. It is easy to see that the payment of unpaid debts for operating expenses, accrued within ninety days, due by a railroad company suddenly deprived of the control of its property, due to operatives in its employ, whose cessation from the work simultaneously is to be deprecated, in the interests both of the property and of the public, and the payment of limited amounts due to other and connecting lines of road for materials and repairs, and for unpaid ticket and freight balances, the outcome of indispensable business relations, where a stoppage of the continuance of such business relations would be a probable result, in case of non-payment, the general consequence involving largely, also, the interests and accommodation of travel and traffic, may well place such payments in the category of payments to preserve the mortgaged property in a large

sense, by maintaining the good will and integrity of the enterprise, and entitle them to be made a first lien."

Counsel for appellants cite the case of Union Trust Company vs. Souther, 107 U. S. 591: 2 Sup. Ct. Rep. 295. The claim prosecuted for priority in that case by Souther Bros. was for the sum of \$532.14 "for supplies." The statement of the case does not make it clear that the supplies were used as part of the current expenses of the road, but leaves the clear inference that they were as a reading of the opinion will show. The size of the claim would indicate the same thing. If they were, the decision is clearly right and in accord with every decision of this court before and since. One thing is clear. The supplies in that case were not sold on the general or personal credit of the Company, were not used for virtually reconstructing the road and the case is not an authority for decreeing priority to appellants' claim.

The case of Union Trust Company vs. Illinois Midland Railway Company, 117 U. S. 134, 6 Supreme Court reporter, 809, is cited by counsel for appellants. I have read this opinion with some care and find that ^{the} only claims passed upon in the opinion, seeking priority over the mortgage bond holders were those of Warring Bros. These claims were denied priority in the court below, and this court after full consideration of the case affirmed the judgement of the lower court. The case is not an authority for any point involved in this appeal. The case of Union Trust Company vs. Morrison, 125 U. S. 591, 8 Supreme Reporter 1004 is cited also. The Syllabus of that case gives in substance all that is decided in the opinion, and which is as follows: "Where the mortgaged rolling stock of a railroad is in peril of seizure under a judgment, and the railroad claiming the judgement to be wrongful, obtains an injunction against such seizure, one who becomes surety on the injunction bond, the injunction having been dissolved, and judgment recovered against him, has an equity to be paid out of the property of the railroad which is sold to the mortgages at the foreclosure sale, especially when they have purchased expressly subject to intervening claims that may be declared paramount, where the receiver has used earnings to increase the *corpus* of the estate, and where the surety has shown an intention to look to the company's property, as well as its personal security by taking a chattel mortgage on certain locomotives."

The above ^{quotation} ~~quotation~~ shows that the decision is not an authority for any point involved in this appeal.

The case of Virginia & A. Coal Co. vs. Central Railroad & Banking Company, 170 U. S. 355 18 Supreme Court Reporter, p. 657, in the last decision of this court within our knowledge on the subject of preferential claims. The opinion in that case was delivered May 9th, 1898. This opinion was delivered so recently we assume the facts of the case and the points decided are fresh in the memory of the members of the court, and will not burden the court with a statement of the case, other than to say

that the claims asserted in that case were for coal furnished by two coal companies to the railway company prior to the appointment of the receiver. Mr. Justice White in delivering the opinion of the court in that case, after stating the case and quoting with approval the opinions of this court in the cases of *Wallace vs. Loomis*, and *Burnham vs. Bowen*, says: (Italics ours).

"The equity thus held to arise when a purchase of necessary current supplies is made by ^{the} owning company, is not in any wise influenced by the fact that the company itself is the purchaser of the supplies, *but it is solely dependent upon the fact that the supplies are sold and purchased for use, and that they are used in the operation of the road; that they are essential for such operation; and that the sale was not made simply upon personal credit, but upon the tacit or express understanding that the current earnings would be appropriated for the payment of the debt.*" And further on he says: "Upon the evidence contained in the record, we hold that the contract upon which both interveners relied—the deliveries of the coal furnished by the Sloss Company being under the contract which had been made with the Virginia Company—was made with the Danville Company, but we conclude from the terms of the contract that the intentions of the parties was that the coal was to be used in the operation of the lines of the Central Company, and that the mining companies did not reply simply upon the responsibility of the Danville Company, but, on the contrary, that the coal companies looked to the earnings of the Central system as the source from which the funds to pay for the coal to be furnished were to be derived." And concluding the opinion, he says "In concluding that the claims of the interveners were entitled to priority of the surplus earnings which arose during the control of the road by the court, we must not be understood as in any wise detracting from the force of the intimations in the recent utterances of this court in *Kneeland vs. Trust Co.*, 136 U. S. 89, 10 Sup. Ct. 950 and *Thomas vs. Car Co.* 149 U. S. 95, 13 Sup. Ct. 824, cases as to the necessity of a court of equity confining itself within very restricted limits in the application of the doctrine that in certain cases a court having a road fund under its control may be justified in awarding priority over the claims of mortgage bondholders to unsecured claims originating ~~to a~~ receivership." In the *Kneeland* case, however, the claim refused priority was based upon an alleged instrument of lease, and was for four months' rental of cars operated on a line of railroad by a receiver appointed at the suit of a judgment creditor, such receiver being succeeded in office by a receiver appointed in the foreclosure proceedings instituted by the trustees of the mortgage bondholders. It was held that the alleged contracts of lease were in substance and effect, "Antecedent contracts of sale" that in those contracts ample provisions had been made by the vendor for his security by stipulation authorizing a retaking of the property upon failure to make payment promptly of the installments of purchase money as they become due, and that the claim against the fund was in reality for a portion of the purchase price of the cars. Under these circumstances the

debt was held not to be embraced "in the few specified and limited cases" in which this court "has declared that unsecured claims were entitled to priority over mortgage debts," and particular attention was called, among other things, to the fact that the receivership at the suit of the judgment creditor was not for the benefit of the mortgage bondholders, so that it could not be asserted that the expenditures of such receivership were payable, in any event, out of the income or corpus of the property; and the fact was also noticed that from the time of the purchase of the rolling stock in question in the suit to the time of the final disposition of the mortgage foreclosure, the receipts did not equal the operating expenses, and there had been no diversion of the current earnings, either to the payment of interest or the permanent improvement of the company. In the Thomas case, claims for rental of cars, which rental had accrued prior to the receivership, were denied priority over the mortgage bonds; but the facts in that case were such as to justify the conclusion that car company contracted, "upon the responsibility of the railroad company and not in reliance upon the interposition of a court of equity." In neither the Kneeland nor the Thomas case were there any intention to question the prior decisions of the court, *which allowed priority to claims based upon the furnishing of essential and necessary current supplies, not sold upon mere personal credit, against the surplus income arising during the operation of the road under the direction of a court of equity.*"

This opinion brings sharply to view the fact that a claim to be entitled to preferential payment must be for current operating expenses and that the material must not be sold or furnished on the individual responsibility or general credit of the railway company. These propositions are repeated in the opinion and are brought so prominently to the front, ^{as} to leave no shadow of doubt as to the views of this court on this important subject. The claims were allowed priority in that case because the evidence showed them to be the purchase price of coal used and consumed in the operation of the road and further that the coal was not sold on the individual responsibility of the railway company. The claim in the case at bar was by the lower courts denied priority because the rail was bought on the general credit of the railway company in unusually large quantities for the purposes of virtually reconstructing the road and because it could not be classed as a current debt. The decisions of the lower court are therefore in harmony with the above case and with all the decisions of this court on the subject.

From the foregoing and indeed from all the cases on this subject it is plain that a claim to be entitled to priority must *in fact* be a part of the current expenses of the road. If it is then it may be entitled to ~~the~~ priority whether the demand for the material or labor was ordinary, great, pressing or imperative. The priority is not made to depend in any case on supply and demand or the imperativeness or needfulness of the labor or mate-

rial or whether it was simply needed, badly needed or very badly needed. And upon the other hand if the claim is found *as a fact* to be not for current expenses, but a general or floating debt of the company or for purposes of general construction it is never entitled to priority whether the demand for the labor or material was ordinary or was great, pressing or imperative. Neither in this case is the right to priority made to turn upon supply and demand or the pressing necessities of the situation. The distinctions between the two classes of claims never run along such lines but always turn on the *class* of the claim. The maritime doctrine of salvage has not been adopted in this class of cases—but has been held by this court to furnish no analogy or aid in determining questions of the character under consideration. So the fact that the rail in this case was badly needed cannot alter the nature of the claim, and change it from that of a general debt to that of a special debt, so long as the facts in the record show that the claim cannot be classed as a current debt, and show that the rail was sold in unusually large quantities on the general credit of the railway company and for virtually reconstructing the road. It is always to the nature of the claim that we look to determine its class. Was it one of the current claims for necessary expenses of operation? If not it is not entitled to priority. This is the whole circuit of the inquiry. How badly the material or supplies were needed cannot be looked to in classing the claim. No case has within our knowledge turned upon that point.

Credit must be temporary and result from the necessities of the business.

Blair vs. Ry. Co., 22 Fed. Rep., 471.

Debt must have been contracted short while prior to appointment of receiver.

Thomas vs. Peoria Ry. Co., 36 Fed. Rep., 808.

Turner vs. Indianapolis Ry. Co., 8 Biss, (U. S.) 315.

Fosdick vs. Scholl, 99 U. S., 235.

Union Trust Co. vs. Ill. Mid. Ry. Co., 117 U. S., 434.

Taylor vs. Ry. Co., 7 Fed., 377.

Miltenberger vs. Logansport R. Co., 106 U. S., 286.

Six months seems to be the general rule, which may be deduced from the authorities, and it is only in cases presenting strong equitable features that back debts of longer standing will be given priority. No exceptional equity seems to be claimed in this case, or if claimed none is shown. In this case the last contract was made sixteen months prior to the first receivership and five years and six months prior to appointment of receiver in this cause. (R. p. 103.)

Second Proposition.

The effect and the only effect of a finding that a back debt was contracted an unreasonable time prior to the appointment

of a receiver is to take the claim out of the preferred column and place it among the general floating indebtedness of the company, and when this is done by a direct finding that the debt was contracted upon the general credit of the company, it is not material whether it was contracted a reasonable or unreasonable time prior to the appointment of a receiver.

STATEMENT.

The master finds that appellants' claim is *not a current debt*, and was contracted on the *general credit* of the company. (R. p. 103.)

Thomas vs. Peoria Ry. Co., 36 Fed., 808.

Manchester Locomotive Works vs. Truesdale, 44 Minn., 115.

Third Proposition.

Before a debt for current supplies will be given priority it must appear that the order appointing the receiver made provision for the payment of such claims or that there has been a wrongful diversion of the current revenues of the road which should or would have been used in the payment of such debt to the payment of bonded interest or permanent improvement of the property covered by the mortgage, and the extent of such priority will be limited to the amount diverted. Neither fact exists in this case.

STATEMENT.

1. There is no provision in any of the orders appointing receivers in causes 185, 198 and 227 for the payment of back debts.

2. There has been no diversion of the income of the road to the payment of bonded indebtedness or permanent improvements which should or would have been used for the payment of appellants' debt either by the railway company prior to receivership of said property or by any of the receivers since. All interest appears to have been paid on bonded indebtedness up to January 1, 1885, when the first default occurred. No interest has been since paid on first mortgage bonds of the Waco division, except \$91,371.00 paid by order of the Court by the receivers in cause 198 on about May 1, 1887, being the installments of interest which matured January 1 and July 1, 1885, and interest thereon to date of payment (R. p. 114.) This is all the interest that has been received by those bond holders for a period of twelve years. The rail in question was sold under two separate contracts; one dated April 26, 1883, under which 5,009 tons of 56-pound rail at \$39.50 per ton were delivered during the months of June, August and September, 1883. (R. p. 100.) The other contract is dated October 30, 1883, under which 8,552 tons of 54 pound rail at \$36.60 were delivered during February, March, April and May, 1884. (R. p. 101.) The contracts of sale provide that the rail is to be paid for in notes at six months with six per cent. interest, with privilege in the Railway Com-

pany to extend time of payment six months longer. In accordance with the terms of these contracts, notes were given and which were renewed and extended from time to time, so that all the notes due petitioner matured after January 1, 1885, and during the months of February, March, April and May. (R. pp. 100 to 101.) Petitioner having extended the time of payment could not in the meantime prior to the maturity of the notes demand payment of said notes, and cannot now complain of interest payments being made before the maturity of its own notes. The record shows that the bonded interest of the railway company was payable semi-annually on January 1 and July 1. Interest was paid January 1, 1883, July 1, 1883, January 1, 1884, and July 1, 1884, by the company. All these payments were long prior to the maturity of petitioner's debt. It can in no sense be said that these interest payments was a diversion of the stream from its natural channel. It cannot be presumed that this money would have been paid appellants but for the interest payment, for at that time the company owed appellants no matured debt. Appellants are therefore estopped by their own contract in first giving time and afterwards extending time of payment from claiming the money used in paying interest on the bonded debts from the date of the sale in 1883 to maturity of the debts in February, March, April and May, 1885.

Our position is that appellants cannot complain of the payment of any valid debt of the company which was in existence when the rail was sold, and of which it had notice, and which matured prior to the maturity of their debts. This would give all interest installments which matured prior to the February, March, April and May, 1885, priority over the debt of appellants and of course would include the installment of interest which matured January 1, 1885. The receivers in cause 185 were appointed February 20, 1885, and the property has been in the possession of receivers in causes 185, 198 and 227 continuously since. As stated above no interest was paid in causes 185 or 227, and of the payments made May 1, 1887, one-half was for interest which matured January 1, 1885, and which matured prior to the maturity of any of appellant's notes, and which appellants must have understood would be paid at maturity. The whole of said interest payment of May 1, 1887, was made on application to the Court in cause 198, to which cause appellants were parties. If appellants were in law or in fact entitled to said fund in preference to the bond holders, in that cause, and on that occasion, was the time and place to have asserted their rights thereto. Besides the order was made without prejudice. On this subject the master finds:

"I find that said order expressly declared that it was 'without prejudice to the rights of defendant or of any intervenor in this cause, or any final decree to be rendered in the same, nothing herein being decided as to the merits of the claim of the defendants, or of intervenors, and this order not in any manner estopping or affecting the rights of any party or intervenor in this cause.'" (R. p. 117.)

If this money was received by the bond holders without prejudice they are surely not to be harrassed in after years in a separate suit with a serious charge that this interest was wrongfully taken from one of the very creditors who was a party to the cause and participated in taking the order. The bonds and mortgage securing same are admitted to be valid and unpaid, and if the bond holder is not protected by the above provision against the charge of diversion in accepting this interest, then it may be truly said that this money was taken with great probability that the act of doing so would be very prejudicial, indeed to the extent of refunding every dollar received with interest thereon at the end of an expensive lawsuit. The order was doubtless intended to provide for the payment of a debt which was conceded to be valid, but that in doing so no precedent should be established as to who was entitled to priority in payment out of the net income or proceeds of sale of the road as a protection to petitioner and other parties and intervenors who were asserting priority over the bond holders, and that the bond holder, on the other hand, in accepting the money, should not be charged with diverting that money from the other claimants. If the above is a valid interpretation of the order it is manifest that no diversion has been shown by way of interest payment.

It only remains to be considered whether there has been a wrongful diversion of funds in the erection of betterments and permanent improvements on the Waco branch. On this subject the master finds:

"I find that no interest has been paid on the bonded indebtedness by either of the receivers in this cause; I find that Alfred Abeel, receiver in this cause, has expended, under the orders of this court, \$46,505.40, for betterments and permanent improvements, from December 10, 1892, to September 3, 1895, consisting of bridges, shops and round houses, car shed, water stations, locomotives, chair car and fencing." (R. p. 109.)

"I find that no part of the income arising from the operation of the road and no part of the proceeds of sales of old rails, old iron, old cars and engines, which was received by the receivers in causes Nos. 185 and 198, ever came into the possession of the receiver in this cause, and the evidence fails to show that any part of the new equipment purchased by the receivers in causes Nos. 185 and 198, as shown above ever came into the possession of the receivers in this cause. The evidence fails to show that any improvements and betterments of the property added to the property of the Houston and Texas Central Railway Company by the receivers in causes Nos. 185 and 198, were made on the Waco and Northwestern division." (R. p. 110.)

"I find that prior to April 6, 1889, no separate accounts were kept of the receipts and disbursements of the Waco and Northwestern division, but the same was operated as a branch of the general system of the Houston and Texas Central Rail-

way Company, and the evidence fails to show what if any, of the expenditures made by the receivers in causes Nos. 185 and 198, for extraordinary repairs, betterments and improvements and for operating and running expenses were made for said Waco and Northwestern division, and what portion for the other division of said Houston and Texas Central Railway Company; and this is true also as to the receipts and incomes." (R. p. 110.)

"I find that the receivers in cause No. 185, had on hand in cash at the opening of business on January 21, 1886, \$175,393.65, but there is no evidence that any part of said fund came into possession of the receivers in this cause." (R. p. 110.)

"I find that the receiver in cause No. 198, had on hand at beginning of business on April 6, 1889, cash amounting to \$215,842.45, but the evidence does not show that any part of said funds came into the hands of the receivers in this cause." (R. p. 110.)

The above findings show that the only betterments added to the Waco branch in the long period of time covering over eleven years, was \$46,505.40 for betterments and permanent improvements from December 10, 1892, to September 3, 1893, consisting of bridges, shops, and round-houses and car shed, water stations, locomotives, chair car and fencing. The first expenditures for these betterments (December 10, 1892) were made nearly eight years after maturity of petitioner's notes and the last (September, 1895) were made over ten and a half years thereafter. At this time, unless suit had been instituted on the notes they would have been long since barred by limitation, and it could not be held that this fund arising from the operation of the road a decade after the rail were furnished was the current revenue which should have been applied to the payment of petitioner's debt. If this were so there would be no current fund available for the payment of current expenses and the necessary improvements from time to time required to keep the road "a going concern." No Court has ever held that expenditures, so far removed by time, place and circumstance from the claimed current indebtedness to amount to a diversion. But, aside from this, these expenditures were all made under the orders of this Court, in this cause, to which appellants have been parties since 1891. The right to order such expenditures and the necessity therefor has been long since determined by the Circuit Court, and such orders estop and conclude petitioner.

The foregoing argument is based on the assumption that it was found by the master that the interest payment of \$91,371.00, in May, 1887, on the Waco & Northwestern division bonds, was made out of the current revenues of the road. On this subject the master finds that the accounts were not kept in such a manner as to indicate the exact fund out of which the interest payments were made, and that no separate account was kept of the

earnings of the Waco & Northwestern division as distinguished from the earnings of the other division. And he nowhere finds that this interest was paid out of the income. (See findings R. pp. 110, 114 and 121.) The same is true as to the expenditures for betterments and new equipment. The master finds that the only expenditures made for that purpose on the Waco & Northwestern division was made by Receiver Abbel after December 10, 1892, and prior to September 3, 1895, and amounted to \$46,505.40. (R. pp. 109-10.) But there is no finding that these expenditures were made *out of the current income*. The finding is simply that this amount of money was used for that purpose. The burden was on appellant to prove that the expenditures, which it is claimed amounted to a diversion of the current income, were, in fact, made from *that fund*. The findings leave appellant's case without equitable support. For the only real equity relied on by appellant to establish the claimed priority, was the alleged diversion of current income from the payment of supply creditors to the payment of interest on the bonded indebtedness and the erection of permanent improvements upon the mortgaged property.

Appellant would not be entitled to recover on the ground of diversion even if that fact were established, because this rail was sold on the "general credit of the company," was no part of the "current supplies," was part of an "usually large purchase" without any understanding that the rail "should be paid for in any particular way or out of any particular fund" and for virtually reconstructing the road. Besides, the findings show that the rail was furnished twelve to thirteen years ago, and there is nothing in the record to show to what extent, if any, the rail enhanced the value of the mortgage security, or that the road has earned a greater net revenue or sold for a greater price as a result of the placing of this rail in the road. There are no findings whatever on these issues. Appellant is in no position to complain of the sudden action of the Court in appointing receivers in cause 185 in February, 1885, for in a short while thereafter appellant intervened in said suit, joined the Southern Development Company in its prayer for a receiver, and in all things ratified the acts of that company. (R. p. 107.)

Case of Bound vs. Ry. Co., 58th Fed., 473, is in point. In that case this same company, the Lackawanna Iron and Coal Company, intervened on precisely the same character of claim as asserted here for the price of steel rails sold to the Railroad Company on a credit of eight months, and the sale was made eighteen months prior to the appointment of the receiver, and said rails were necessary to the maintenance of the road, and were sold on the promise of the president of the road that they were to be paid for out of the earnings, but this promise was not fulfilled. The notes were extended from time to time, and during the interval before the maturity of the first note \$33,000.00 was paid on account of interest due the mortgage bond holders.

It was claimed by intervenor there, as is claimed here, that because its debt was for material which went into the road, improving its condition, and because there had been a diversion of the current debt fund to the payment of interest on mortgage bonds, it was entitled to displace the bond holders to the extent of such interest payment. The claimant prevailed in the lower Court, and the displaced bond holders appealed to the Circuit Court of Appeals. Chief Justice Fuller acting as Circuit Justice, and Judge Hughes and Morris composed the Court, and in passing on and deciding the claim of intervenor there asserted, the Court say: "The rule giving preference to current expenses incurred on the faith of the earnings of a railroad shortly before the appointment of a receiver has never been carried so far. The debt of the Lackawanna Company was an ordinary merchandise debt. The road being heavily mortgaged all that any unsecured creditor had to look to was the earnings. The immediate earnings, it is clear, the Lackawanna Company did not look to, as the sale was on credit of eight months. It must be inferred, therefore, that it was expected that interest on the mortgage debts was meanwhile to be paid during the running of the credit, otherwise a foreclosure would have been imminent within three months after the sale of steel rails was made. The claim is quite different from those ordinary and necessary expenses of operating a railroad contracted but a short time before a receivership, and which by the sudden action of a Court in appointing a receiver, are left unpaid."

To repeat, we believe we have two sufficient answers to this claim of diversion. In the first place, it must be shown that appellants' claim is of the preferential class before they can avail themselves of the doctrine of diversion, or, in other words, claim that there has been a diversion, as we do not understand that a general creditor who is not protected by the peculiar equity which brings his case within the protection of this court is in a position to complain that other creditors have been paid certain amounts on their debts. In the second place it appears from the master's findings that the accounts of the receivership were not kept in a manner so that it can be determined out of what fund this payment of interest was made. On this subject the master finds:

"I further find that the accounts of said railway company were not kept in such a manner as to indicate the exact fund out of which the interest on said first mortgage bonds of the Waco & Northwestern Division were paid, or the exact fund out of which the interest upon the bonds of the other divisions was paid." (R. p. 121.)

As to the erection of betterments on the mortgaged premises, the findings are of the same inconclusive nature. The master nowhere finds that any improvements were erected and paid out of the *income* of the road. He finds on this subject as follows:

"I find that Alfred Abeel, receiver in this cause, has expended under the order of this court, \$46,505.40 for betterments and permanent improvements from December 10th, 1892, to September 3rd, 1895, consisting of bridges, shops and round-house, car shed, water stations, locomotives, chair car and fencing." (R. p. 110.)

"I find that no part of the income arising from the operation of the road and no part of the proceeds of sales of old iron, old rails, old cars and engines, which was received by the receivers in causes Nos. 185 and 198, ever came into the possession of the receiver in this cause, and the evidence fails to show that any part of the new equipment purchased by the receivers in causes Nos. 185 and 198, as shown above, ever came into the possession of the receivers of this cause. The evidence fails to show that any improvements and betterments of the property added to the property of the Houston & Texas Central Railway Company by the receivers in causes No. 185 and 198, were made on the Waco & Northwestern division." (R. p. 110.)

It will be observed that he does not find that these betterments were paid out of the revenue of the road. The record shows that the mortgage covered a large landed property, aggregating 228,622.28 acres of land besides vendors' lien notes aggregating \$107,145.66, still on hand, and which has during all this time been in the hands of the receiver. For aught that appears, the small amount of improvements erected by Abeel, the present receiver, were made out of funds arising from the sale of lands, or collection of land notes covered by the mortgage. In such case no diversion could exist. At least the burden was on appellants not only to allege but to prove a diversion. The Circuit Court of Appeals of the sixth circuit, in the case of Central Trust Co. vs. East Tenn. V. & G. Ry. Co., 80 Fed. at page 626, disposes of a claim that there had been a diversion upon a record substantially similar to the record in this case, and say: (*Italics ours.*)

"But it is also shown that, during the same period, money was borrowed on open account, more than sufficient to equal the diversion complained of, which went into a common treasury, from which operating expenses, preferential claims, interest, and improvements were paid, without any definite showing as to whether the borrowed money was applied to the payment of interest and improvements, or current income debts. Under this system of bookkeeping, the addition of the borrowed money to the income arising from operation showed a substantial surplus after payment of the great mass of income debts, and all disbursements on account of interest upon the two mortgages foreclosed, as well as upon improvements in the roadway. Prior to the period covered by the maturity of the appellant's claims there was a surplus of gross earnings over all operating expenses; but it cannot be contended that the company was under any obligation to future creditors to accumulate a surplus to meet possible deficiencies in the income to meet future income debts, or that it was improper to apply such surplus in

payment of interest. *St. Louis A. & T. H. R. Co. vs. Cleveland C. C. & I. Ry. Co.*, 125 U. S. 658-675, 8 Sup. Ct. 1011. Whatever diversion there may have been of income to payment of debts or liabilities, not properly debts of the income, seems to have been more than reimbursed by the money borrowed. *The burden is upon complainants to show that there has been a misappropriation of earnings to the improvement of the mortgaged property, or to the payment of interest, before the mortgagees can be justly called upon to reimburse the fund applicable to debts of the income in consequence of such diversion.* If interest was paid or improvements made out of borrowed money, then there was no diversion; or if made out of gross earnings, and the latter was reimbursed by borrowed money, the diversion was made good. The abstracts showing income from all sources and disbursements upon all accounts are somewhat complicated, in consequence of the mode of bookkeeping adopted. The commissioner and court below concurred in reporting that there was no diversion shown. In the absence of every cogent evidence of mistake of fact, or of some error of the law, the finding of fact by the commissioner must be accepted as final. *Emil Kiewert Co. vs. Juneau*, 24 C. C. A. 294, 78 Fed. 708; *Kimberly vs. Arms*, 129 U. S. 512-524, 9 Sup. Ct. 355, *Tilghman vs. Proctor*, 125 U. S. 136, 8 Sup. Ct. 894; *Turley vs. Turley*, 85 Tenn. 256, 1 S. W. 891."

On what has been said, we are content to leave the case in the hands of this court on the question of diversion.

Fourth Proposition.

Appellants are not entitled to a ratable distribution of the fund in question.

This brings us to the further inquiry; that is, whether appellants have shown that they are entitled to have the decree appealed from reversed and the case sent back so that they may demand pro rata division of the income in the hands of the receiver among all the creditors? This proposition is based on the claim that the mortgage bonds are not secured by a lien on the income after possession was taken. The Circuit Court of Appeals of the fifth circuit, on the same day the opinion was delivered in this case, held in the case of *Geo. E. Downs vs. Farmers' Loan and Trust Company, et al*, that the mortgage in this case did cover the income. (79 Fed. Rep. at page 221.) That case appears to be the conclusion of this question.

There is therefore no warrant for the assumption that no one had a lien on the fund that was used in paying interest on the bonds. For the purposes of this point it may be conceded that the interest was paid out of current income as claimed by petitioners. The findings of the master show that on February 16th, 1885, the Southern Development Company filed its original bill of complaint against the Houston & Texas Central Railway Company in cause No. 185, and that upon this bill receivers,

Clark and Dillingham, were appointed. That on March 31st, 1885, the Farmers' Loan & Trust Company filed its petition in said cause No. 185, praying to be made a party thereto, averring, among other things, that it was trustee under several separate mortgages executed by defendant railway company, and naming among them the mortgage declared herein. That the prayer of said petition was granted, and on April 8th, 1885, said court entered an order in said cause No. 185, allowing the Farmers' Loan & Trust Company to become a defendant in said suit; and further ordering that it may demur, plead or answer therein on or before the rule day in June, 1885. The record shows that demurrers were filed to the bill of complaint of the Southern Development Company by Easton & Rentool, trustees in one or more of the mortgages executed by defendant railway company, and on May 26th, 1886, these demurrers were in all things sustained, and the entire bill and the supplemental bill of the Southern Development Company was dismissed. Upon the dismissal of these bills in cause No. 185, all the property was transferred to receivers in consolidated cause 198. No other action was thereafter taken in cause 185, but causes 198, 199 and 201 were consolidated, and proceeded to judgment and foreclosure as consolidated cause 198. The consolidation of these causes took place on May 26, 1886, and the causes were filed a few months prior to this. The bills in causes 198, 199 and 201 were bills to foreclose three mortgages given by the Houston & Texas Central railway Company on its railway and properties. One was on the main line, the other on the Austin branch, and third was a general mortgage on the whole system.

Neither the bills of complaint or the mortgages declared on in causes 198, 199 and 201 are in the record, and for that reason it cannot be determined whether these mortgages, in terms, covered the income after possession was taken. But it is clear that at the suit of the trustees in the mortgages declared on in causes 198, 199 and 201, all the property, income, rents and profits of Houston & Texas Central Railway was, on May 20th, 1886, placed in the hands of receivers. By placing the property in the hands of receivers the complaints in those bills made an equitable levy upon the rents and profits to accrue from the operation of the road by the receivers. (Sage vs. Memphis, etc. R'y Co., 125 U. S., 365.) It is very likely the mortgages were drawn in the usual manner of such mortgages, giving a lien on the income after possession is taken. As appellants failed to bring up with the record these mortgages, it may be assumed that if here they would be of value to them. It, therefore, appears with reasonable certainty, that there was a lien on the income of the road and the whole system, after possession was taken at the suit of complainants in causes 198, 199 and 201 on May 26th, 1886, and continuously thereafter, and this lien was in favor of the mortgaged bondholders, secured by the mortgages declared on in the above three causes.

The interest payment of \$91,371.00 to the bondholders secured by mortgages on the Waco & Northwestern branch so

much complained of, was not made until May 1st, 1887, nearly a year after the receivers appointed in consolidated cause 198 had taken possession. This fact is perfectly manifest from the record. Under these circumstances, and while the whole net revenue of the road was under lien to secure the mortgages declared on causes 198, 199 and 201, the complainants in these causes jointly with the trustee in the first mortgage on the Waco & Northwestern branch, applied to the court to have the coupons which matured on January 1st and July 1st, 1885, paid on all the bonds. The prayer of this petition was granted, and the interest was paid on all the first mortgage bonds, and the interest paid ~~to~~ these bondholders amounted to \$91,371.00. As it appears that appellants claim is not of the preferred class, and as it further appears that use of the current income for the payment of interest was with the express consent and at the request of the bondholders holding a lien on the very fund used, and who alone could complain, there was certainly no "diversion" of which appellants could complain.

Let us view the matter from another standpoint. Suppose this \$91,371.00 was today returned to the receivers in consolidated cause 198, and appellants should apply to have it divided on the principle that equality is equity, and demand a *pro rata* distribution? Would its petition be granted? No. Why?

Because they would be shown that the fund was net income which arose from the operation of the road by the receivers appointed in consolidated cause 198, and that the bondholders either held a lien on this income by the terms of their mortgages after possession was taken, or by the virtue of the equitable levy through the appointment of the receivers, and the whole fund would go to the bondholders in those mortgages, and appellants after the labor and pains of much hard sailing, would be found stranded upon a barren shore, penniless and forelorn. If the bondholders, secured by mortgages declared on in cause 198, chose to invite the bondholders in this cause to participate in a fund to which they had no legal or equitable right, and which belonged to the bondholders in cause 198, that was a matter which could not concern appellants. Appellants were not thereby deprived of a right of any description. Not one dollar of the money paid to the Waco & Northwestern bondholders could have been recovered by petitioners, if the interest had not been paid. In a free fight, under the most favorable conditions, the able counsel for appellants could not hope to successfully engineer this scheme of ratable distribution. It is a bare, naked falacy. It is a delusion. This court will not send this case back to the court below to enable counsel to chase a phantom.

We beg to call attention to the fact that this claim for *pro rata* distribution is an afterthought. No mention of such a claim can be found in appellant's petition of intervention. (R. pp. 75 to 88.) The claim was prosecuted in the lower court upon the demand that appellants were entitled to priority over the bondholders.

The contest was with the bondholders alone. No other party but these two could have an interest in that controversy. But in the doctrine of general equitable distribution now urged, all the creditors must be brought in and a general adjustment take place. This idea was the first time advanced in the Circuit Court of Appeals on page 24 of appellants' brief in that court. It had not been, prior to that time, a matter of any concern to appellants whether the bondholders had a lien or not. They claimed a lien prior and paramount to the best and highest. There is no assignment of error based upon this idea. It is a new tack, based upon the fertile imagination of the able and ingenious counsel who made it, but has no substantial foundation in any issue in this case.

But suppose it be conceded that the fund used to pay the \$91,371.00 interest was not net income, and that nobody had a lien upon or charge against it. This concession aids appellants not in the least. In the first place there is neither pleading or parties before the court to warrant the relief demanded. But the fatal answer to appellants' scheme for equitable distribution, by requiring the bondholders to refund the \$91,371.00, and take their share ratably, is that it is nowhere shown that upon the division ~~provision~~ that the bondholders would be ^{entitled} to less than they have already gotten. The record shows that the principal of the indebtedness due to these bondholders is over a million dollars. That the bonds bear interest at 7 per cent. per annum. That the only money paid them during a period of over 12 years, from July 1st, 1884, to this date, is the pittance of \$91,371.00, and it is solemnly and earnestly demanded that they be required to return that, so that appellants may go back to the lower court and get together all the creditors, find out what each has received on his claim, and have a general division, and this, too, some ten years after the final decree of foreclosure has been entered in consolidated cause 198; the property all sold, and the proceeds distributed to thousands of creditors who are scattered to the four winds of heaven.

But this is not all. If for a moment it ^{be} ~~we~~ ~~re~~ conceded the appellants ever had the remotest interest in the \$91,371.00 paid on the bonds secured by the mortgage foreclosed herein, and had an apparent right to complain of this payment, we beg to call attention to the manner in which the holders of these bonds were treated by the receivers in causes Nos. 185, 198 and 227, until Alfred Abeel was appointed receiver to succeed Mr. Dillingham in December, 1892. Summarized the treatment was this: During the time the entire system of the Houston & Texas Central Railway, which included the Waco branch, was in the hands of receivers from February, 1885, to December, 1892, there was spent in betterments and permanent improvements by the receivers \$763,404.03. Not a dollar of this was put on the Waco branch. That branch is about one ninth in mileage of the entire system, and was justly entitled to one ninth of the betterments, which would be \$84,823.67. It not

only received no betterments by the receivers, but the old rail taken up by the company from that branch was on hand when the receivers were appointed, and was by them sold for \$38,480.00 net. The mortgage, without doubt, covered these rails. The Waco branch is therefore entitled to an equity equal to these two amounts, or the sum of \$123,302.67 in the proposed pro rata distribution. These equities are superior to the claim of any unsecured general creditor like appellants. This amount must, therefore, be deducted from the imaginary general fund proposed by appellants and placed to the credit of the Waco branch and it is only the balance left after this deduction is made that will be subject to the demanded equitable pro rata distribution. This amount would be more than sufficient to pay for all the rails laid down on the Waco branch out of the Lackawanna purchases, as the principal of the sum demanded against that branch is only \$105,547.15, as this amount does not bear interest. (Thomas vs. Car Co., 149 U. S. 95.)

From this showing, we may reasonably conclude that if the demand of appellants was granted and the case sent back for pro rata distribution, it would avail them nothing.

Fifth Proposition.

Though it may appear that appellants claim on some of the grounds asserted in whole or in part, is entitled to an equitable priority over the mortgage bond holders, such priority will not be decreed in this case, but appellants will be remitted to their intervention in cause No. 198, because (1) it would be inequitable and unjust to charge the proceeds arising from the sale of the road—made more than eleven years after the purchase of said supplies—and the net revenues arising from its operation from five to eleven years thereafter, with payment of such debt, and (2) it appears that the receivers in causes Nos. 185 and 198, from February 20, 1885, to April 6, 1889, a period of over four years, immediately after petitioner's debt matured, operated the whole H. & T. C. system, including the Waco branch, took all its revenues and profits during these four years, took 2,960 tons of old iron rail from the Waco branch and disposed of same at a price of \$13.00 per ton, aggregating \$38,480.00, used the proceeds from the sale of this rail and the revenue of this branch for the purchase of new cars, locomotives and other equipment and the erection of betterments and permanent improvements of the main line and Austin branch, and (3) it appears that this branch during these four years received no betterment or permanent improvements, and the receivers in this cause received no part of the new cars, locomotives and other new equipment purchased by the receivers in causes 185 and 198 and have never come into possession of any of the revenues arising from the operation of said road during the years 1885 to 1889 or the proceeds from the sale of said old iron rail, and because the bond holders secured by the mortgage declared on herein asked no equitable relief in said causes, 185 and 198, and received no part of the proceeds of the sale of the road in said causes.

STATEMENT.

On the subject here discussed, see master's finding No. 16. (R. pp. 109-12.)

On the subject of receipts and expenditures of the entire system by the receivers in causes Nos. 185 and 198, the master finds as follows:

"I find that during the receivership of Clark & Dillingham, in said cause No. 185, they received from the operation of the Railway company revenues, and expended for operating expenses, taxes, etc., the following amounts, to-wit:

Amount received from February 23, 1885 to January 21, 1886, two million, seven hundred and fifty-eight thousand, four hundred and eighty-seven and 40-100 dollars.....	2,758,487.40
Operating expenses, taxes, etc., same period.....	2,137,322.44

Balance or surplus.....	621,164.96
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Amount received from January 21 to July 10, 1886, one million, one hundred and forty-three thousand, seven hundred and thirty-one and 05-100 dollars.....	1,143,731.05
For operating expenses, etc., for the same period..	1,341,753.85

Leaving a deficit for this period of.....	\$198,022.80
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And leaving a net balance from the operation of said railways from February 23, 1885, to July 19, 1886, of.....	\$423,142.16
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XIX.

"I find that when said Clarke & Dillingham took possession of the property of the defendant railway company on February 23, 1885, they received in cash \$30,416.34.

That they collected asserts of the company as follows, to-wit:

Traffic balances and other claims.....	118,730.08
Sales of old rails on hand February 23, 1885.....	110,275.00
Sale of old cars.....	6,500.00

Total.....	\$265,921.42
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Amount expended in paying liabilities of the defendant Railway Company.....	\$23,274.20
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Interest paid upon the first mortgage bonds of the company, being interest due January 1, 1885, to July 1, 1885.....	751,438.15
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Amount expended for new steel rails.....	\$245,793.64
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Amount expended in payment of certain car trust notes.....	125,695.44
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Amount expended for new passenger coaches, baggage, mail and express cars, etc., and locomotives 265,696.33

Amount expended by said receivers for right of way, fencing, track, real estate, depot, roundhouse, foundry and pattern house at Houston..... 126,218.62

Total.....\$1,536,116.38

"I find that the amount expended as above, \$384,026.20, was expended under the receivership of Messrs. Clarke & Dillingham."

"The above statement shows receipts and expenditures to January 9, 1888, the date when Master Winter, heard the evidence on this intervention in cause No. 198, but no proof has been offered before me, showing the receipts and disbursements of the receivership in said consolidated cause since said hearing before said master on January 9, 1888."

XXI.

"I find that said Easton and Rintoul and Dillingham during their receivership realized out of proceeds of sale, or collection of old assets of the defendant company, the sum of \$135,889.70,"

XXII.

"I find that the receivers in cause No. 198 received from the receivers in cause No. 185, the of \$138,751.37 in cash."

"I find that the receivers in consolidated cause No. 198, after they took possession of the assets of the Railway Company on July 10, 1886, and up to the time of the filing of the report of master Winter, paid liabilities of the receivers Clark & Dillingham, taxes, outstanding vouchers, pay rolls, traffic balances, \$221, 421.32, and collected from the amount due said Clarke & Dillingham as receivers in cause No. 185, \$39,016.69."

The above statement shows that the receivers in cause No. 185 expended for betterments as follows:

Amount expended for new steel rails..... \$245,793.64

Amount expended in payment of certain car trust notes 135,695.44

Amount expended for new passenger coaches, baggage, mail and express cars and locomotives..... 265,693.33

Amount expended for right of way, fencing track, real estate, depot, roundhouse, foundry and pattern house at Houston..... 126,218.08

Making a total of..... \$763,404.63

This entire amount, \$763,404.03, was expended in making betterments and improvements, and the purchase of new equipment, etc., on the main line and Austin branch, and no benefit thereof has ever accrued to the Waco branch. The above amount was undoubtedly paid out of the current revenue of the road, and the Waco branch was entitled to its proportionate share. The findings show that no separate account was kept and in the absence thereof, the only equitable division would be on the mileage basis. The Waco branch is about one-ninth in length of the mileage of the entire system and would be equitably entitled to receive out of the above fund \$84,822.67 in betterments and permanent improvements when in fact it received none. In addition to the above statement the findings show that the receivers in cause No. 185 sold 2960 tons of old rail taken from the Waco branch, on which these bond holders had their mortgage, at \$13.00 per ton, making an aggregate of \$38,480.00. The findings show that no part of this fund has ever come into the hands of the receivers in this cause. This amount added to the above sum of \$84,822.67 makes a total of \$123,302.67, that has been wrongfully (as against these bond holders) taken from the Waco branch, and used in the erection of improvements upon the main line and Austin branch. The findings show that 6.2 miles of the Waco branch was laid with rails furnished under the first and second contracts, but no proof was introduced showing what proportion was furnished under each. The findings show that all rails furnished under the first and about one half furnished under the second contract were paid for by the Railway Company prior to any receivership over the property. Such being the findings, no amount has been shown to be unpaid to appellants for the 6.2 miles. The findings show further that 30.8 miles of the Waco branch was laid with rails furnished under the third contract, being the 54-pound rail, and that it requires 84.86 tons of said rail to lay a mile of track, which makes 2,613.68 tons of rails to lay 30.8 miles. The purchase price of this rail is \$36.60 per ton, making a total of \$94,560.68, the original cost price of the total rail unpaid for on the Waco branch. Deducting this amount from the \$123,302.67 leaves an excess of \$28,741.99 that has been wrongfully taken from the Waco branch and appropriated and used on the main line and Austin branch for permanent improvements and betterments, after fully paying for all steel rails unpaid for on the Waco branch. These figures show that a great wrong has already been committed to the extent of over \$28,000.00 and if the fund now in Court should be used in the payment of the 30.8 miles of steel rail another and a greater wrong by far would be committed, but should the receivers in cause No. 198 be required to pay for these rails justice to that extent would be attained.

The foregoing makes it apparent that the appellants should be remitted to their intervention now pending and undetermined in said cause No. 198. The lower court still has juris-

diction over both causes, and entire control of these interventions.

These views were urged upon the attention of the trial Court and it may be that they had the desired influence in the termination of the case. There is no assignment of error covering this feature of the case.

Sixth Proposition.

Appellants allege as one of the grounds of priority that there is a provision in the mortgage declared on allowing the trustee, in case it takes possession of the property under the terms of the mortgage, to pay the floating indebtedness of the company, and that it relied on said provision in selling the rail to the defendant Railway Company. But there is, in fact, no such provision in the mortgage.

STATEMENT.

On this subject the master finds as follows:

"I find in the mortgage given by the Houston and Texas Central Railway Company to the Farmers' Loan and Trust Company, trustee, dated June 16, 1873, being the same mortgage declared on herein, the following provisions:

"And in case the said Houston and Texas Central Railway Company shall fail to pay the principal, or any part thereof, or any installment of the interest, or any part thereof, on any of said bonds at any time when the same shall become due and payable according to the tenor thereof and for sixty days after having been demanded, it shall be competent for the said trustee, its successors or assigns, to enter upon the said railway and premises and property herein conveyed, by its attorneys and agents, and take possession of same without let or hindrance of the said first party and every part and parcel thereof, and the appurtenances, and appoint an agent to operate and manage the same, and receive the revenue and income thereof, applying the said funds, after deducting taxes, necessary expenses and counsel fees, to keep the same in good order and repair, and the surplus to pay the principal and interest of all the bonds which may be due and outstanding, and secured hereby, pro rata, and thereafter, to the payment of any contributions due to the sinking fund herein established. And upon the request of the holders of one-fifth in amount of the bonds so in default which may be at any time outstanding under this deed of trust, it shall be the duty of said second party by its president, or agent duly appointed in its behalf, to enter upon and take actual possession, with or without entry, or foreclosure of said railway and property herein described, and all and singular each and every part and parcel thereof, and assume its management until the arrears of both principal and interest be paid, or the property sold, as herein described, re-

ceiving the rents, revenue and income thereof and applying them in the same manner as above stated.

"It is, however, expressly agreed that the said party of the first part may dispose of the current net revenues and income of all the said property and railway hereby conveyed in such a manner as it shall deem best, until default shall be made in the payment of the interest or principal of said bonds, or of any one or more of them, and shall have the right to sell and dispose of any of such real estate or other property as it may own or acquire, which may not be needed or acquired for the purposes and business of the said Waco and Northwestern division, except in the case of the six thousand acres per mile of completed road, and which sale and conveyance of such outside property shall transfer the said property and title free from encumbrance of this mortgage or deed of trust, and to change its tracks and make any and all alterations necessary for the benefit of the same."

"I find that there is no provision in said mortgage, that the trustee may, if it acquires possession of said railway under said mortgage, pay any floating debt or debts, of said company out of the gross earnings of said railway." (R. pp. 110 to 111.)

This suit was filed for the trustees for the mortgage bond holders in the mortgage declared on herein on April 6, 1889, and at the suit of said trustee this Court placed the railroad and other property covered by the mortgage in the hands of a receiver, complainant's bill setting up the above provision contained in the mortgage declared on, claiming a lien on the corpus of the property, and the earnings of the road after the same was placed in the hands of the receiver. Appellants did not intervene in this cause until more than two years after, and and on to-wit: November 3, 1891, simply setting up its priority, and nothing more.

AUTHORITIES.

Dow vs. Memphis & Little Rock R. Co. 124 U. S. p. 652.

(S. C.) 33 Am. & Eng. R. R. Cases, p. 12.

Sage vs. Memphis & Little Rock R. Co., 125 U. S., 361.

(S. C.) 35 Am. & Eng. R. R. Cases, p. 40 and cases therein cited.

Argument.

The merits of appellant's claim for priority is made to rest partly upon the supposed existence of this clause in the mortgage. From this allegation it plainly appears that appellants when selling these rail and extending the time, fully recognized that no superior equity existed over the mortgage, or if any existed it was not relied on. Instead of selling these rail upon the belief that priority would be given upon principles of equity, appellant Lackawanna Company seems to have made the sales with full knowledge of the existence

of the mortgage, and with the understanding that a contract had already been made for its benefit and perfect protection, in that the mortgage contained a clause which required appellant's debt to be paid in any event. This allegation not only shows upon what security appellant relied, but it shows with equal clearness, the *rank* and *character* of appellant's claim. It shows that appellant, in selling the rail and in placing reliance upon this supposed clause understood its claim to be a mere "floating debt," for the supposed clause relied on provides, according to the allegation, for the payment of "floating debts" only. But this particular mortgage contained no such provision. The foundation having failed the superstructure cannot stand. The evidence shows that a number of mortgages given by defendant company were in existence at this time. It is probable that one or all the others contained some such stipulation. Be this as it may, by the allegation above we are given appellant's own version of the rank of its claim, and the security upon which the rail was sold. Having relied on that security no other can now be claimed in the present condition of the record. "The express mention of one thing implies the exclusion of another," is a legal maxim which controls the language of this pleading. We concede that this is not a rule amounting to estoppel. The petition could have been amended and a different set of facts alleged, and if true, been proven. But nothing of the kind has occurred. No amendment, no change. The case went before the master and trial court and is brought here claiming and asserting, in the strongest language, that the mortgage contains this clause and that appellant relied on the contract therein made for its benefit in selling the rail, has in all things accepted its terms and conditions, and bases its suit thereon. The allegation makes a case of a lien created by express contract for the benefit of "floating debts," with an unqualified acceptance by appellant. If he relied on this supposed express contract he did not rely on the equity asserted by the assignments of error. But the master finds "that both seller and buyer expected the debts to be paid from the *net* income of the railway." (R. p. 104.) This understanding that the claim was to be paid from the *net* income, as distinguished from the current or gross income, effectually took this claim out of the preferred column and placed it among the general floating indebtedness of the company. This, in connection with the further finding of the master, that the rail was sold on "the general credit of the company," that it "was not a current debt," and that the "purchase was of an unusually large amount of rail," "without any stipulation that security should be given by the defendant company, or that payment therefor should be made out of any particular fund or in any particular way," and for virtually reconstructing the road, taken in connection with the above allegation, that the rail was sold relying upon the supposed terms of the mortgage, rendered the lower courts powerless to prefer appellant's claim.

Seventh Proposition.

Appellants would not be entitled to priority by virtue of the laws of Texas as claimed, because the only law of that state that pretended to give the claimed priority has long since been declared by the Supreme Court of Texas to be unconstitutional.

Giles vs. Stanton, 86 Texas, 620.

Receivers vs. DuBose, 87 Texas, 78.

In conclusion, we beg to quote from a few additional cases on the subjects discussed in this brief. In the case of Blair vs. Ry. Co., 22 Fed. Rep. 474, Mr. Justice Brewer has drawn a clear distinction between sales ~~of~~ supplies made on time voluntarily extended to the road and for stated periods and those made on temporary credit and for current expenses resulting from the peculiar nature of railroad business, affirming that business of such magnitude cannot be transacted on a cash basis, and that in the very nature of this business, *temporary credit* is indispensable. He says:

"The idea which underlies them, I take to be this: That the management of a large business, like a railroad business, cannot be conducted on a cash basis. Temporary credit in the very nature of things is indispensable. Its employees cannot be paid every month. It cannot settle with other roads its traffic balances at the close of every day. Time to adjust and settle these various matters is indispensable. Because in the nature of things this is so, temporary credit must be taken as assented to by the mortgagees, because both the mortgagees and the public are interested in keeping up the road, and having it preserved as a going concern, and whatever is necessary to accomplish this result must be taken as assented to by the mortgagees."

In Kneeland vs. Am. Loan Co., 136 U. S., 97 and 98, Mr Justice Brewer used this very forcible language in reference to the character of claims here asserted: "Upon these facts, we remark, first, the appointment of a receiver vests in the Court no absolute control over the property, and no general authority to displace vested contract liens. Because in a few specified and limited cases this court has declared that unsecured claims were entitled to priority over mortgaged debts, an idea seems to have obtained that a Court appointing a receiver acquires power to give such preference to any general and unsecured claims. It has been assumed that a Court appointing a receiver could rightfully burden the mortgaged property for the payment of an unsecured indebtedness. Indeed, we are advised that some Courts have made the appointment of a receiver conditional upon the payment of all unsecured indebtedness in preference to the mortgage liens sought to be enforced. Can anything be conceived which more thoroughly destroys the sacredness of contract obligations? One holding a mortgage debt upon a railroad has the same right to demand and expect

of the Court respect for his vested and contracted priority as the holders of a mortgage lien on a farm or lot, so, when a Court appoints a receiver of railroad property, it has no right to make that receivership conditional on the payment of other than those few unsecured claims which, by the ruling of this Court, have been declared to have an equitable priority. No one is bound to sell to a railroad company, or to work for it, and whoever has dealings with a company whose property is mortgaged must be assumed to have dealt with it on the faith of its personal responsibility, and not in the expectation of subsequently displacing the priority of the mortgage liens. It is the exception, and not the rule, that such priority liens can be displaced. We emphasize this fact of the sacredness of contract liens, for the reason that there seems to be growing an idea that the chancellor in the exercise of his equitable powers, has unlimited discretion in this matter of the displacement of vested liens. *Railroad Co. vs. Railroad Co.*, 125 U. S., 658, 673. So that these intervenors acquire no right of priority by virtue of their antecedent contracts of sale."

To the authorities cited above, we add the following:

1. On the question of allowing back debts of longer standing than six months:

20 Am. & Eng. Ency. of Law, p. 425 and cases cited.

Blair vs. Ry. Co., 22 Fed. Rep., p. 471.

In re Kelley, 5 Fed. Rep., p. 846.

On the question of the propriety of a Court of equity to give claims of the character herein asserted priority over a prior mortgage:

Forman vs. Central Trust Co., 71 Fed. Rep., p. 776.

Railway Company vs. Cowdy, 11 Wall, 482.

Central Trust Co. vs. Chattanooga Ry. Co., 69 Fed. Rep., 295.

Thompson vs. Valley Ry. Co., 132 U. S., 68.

Farmers & Merchants Nat. Bk. vs. Ry. Co., 36 S. W. R., 131.

Toledo Ry. Co. vs. Hamilton, 134 U. S., 296.

Trustees vs. Ry. Co., 2 Wood, 542.

Denison vs. Ry., Co., 4 Biss, 416.

High on Receivers, Sec. 394a.

Express Co. vs. Ry. Co., 99 U. S., 191.

Turner vs. Ry. Co., 8 Biss, 315.

Miltenberger vs. Ry. Co., 106 U. S., 286.

Trust Co. vs. Souter, 107 U. S., 591.

Burnham vs. Bowen, 111 U. S., 776.

L. C. & N. Co. vs. Ry. Co., 29 N. J., Eq., 252.

In re Kelley, 5 Fed. Rep., 846.

Bridge Co. vs. Douglas, 12 Bush, 673.

We submit with confidence, that appellants have not shown that they are entitled to priority of payment, either out of the proceeds of sale or net income arising from the operation of the road, or that there is error in the degree appealed from and we request that it be affirmed.

The foregoing brief together with what we say in our briefs filed in the circuit court of appeals—copies of which are filed in ~~the~~ court—sufficiently presents our views of the facts of the case and ~~this~~ law arising thereon. We therefore pass to the consideration of another proposition—,namely. That appellant's petition for priority must in the end be denied because if the claim ever belonged to the preferential class it has long since been paid off, merged and extinguished by the terms of the purchase. All the facts bearing upon this point are not in this record proper and the point is presented and asked be considered only in the event this court should conclude that appellants are entitled to priority in the payment of their claim over the bond holders and then only as grounds for ~~reversing~~ ^{reversing} and remanding instead of ~~reversing~~ ^{reversing} with directions to render. We are quite sincere when we say we have no fears of such a result we feel it not out of place to call attention to the facts as they have been unfolded and brought to light in the many branches of litigation which have grown out of the main case in which appellants intervened and prosecuted their claim for priority. We will not burden this court with a long and tedious statement. Suffice it to say that there has been two sales of the railway properties held by the court through its receivers. The first was a foreclosure sale under a junior mortgage and the last a foreclosure sale under the first mortgage. At the first sale one Geo. E. Downs became the nominal purchaser, and at the second, Wilbur F. Boyle became the nominal purchaser, but both purchases were in fact made for the appellant Pacific Improvement Company, the owner of the Lackawanna claim. By the terms of the final decrees under which both sales were made the purchaser was in terms required to pay the Lackawanna claim. The facts as to who were the real purchasers at said sales have come to light since this case was decided by the Circuit Court of Appeals. But the facts are quite clear and the Circuit Court of Appeals in deciding several appeals taken out of the main case since this appeal have recently held that the appellant Pacific Improvement Company as a part of their purchase and in addition to the sum bid, agreed to pay the Lackawanna claim—the very claim being prosecuted in this court by the Pacific Improvement Company for priority over the mortgage bondholders. On this subject that court say:

"The record shows that the Pacific Improvement Company is the real party in interest represented in these several appeals, that Company being the purchaser represented by Wilbur F. Boyle, and the owner of the 614 bonds, which said Boyle represents, and the owner of the Lackawanna claim, set up as a lien prior to that of the first mortgage bonds; that the purchaser at the sale under the decree, and as a part of the consideration, and in addition to the sum bid, took the property upon the express condition that he would pay and satisfy, among others, the Lackawanna claim; that the reservation of the sum of \$187,000, out of the earnings of the road to await the decision

of the Supreme Court of the Lackawanna claim is in the direct interest of the appellants." 88 Fed. Rep. p. 930.

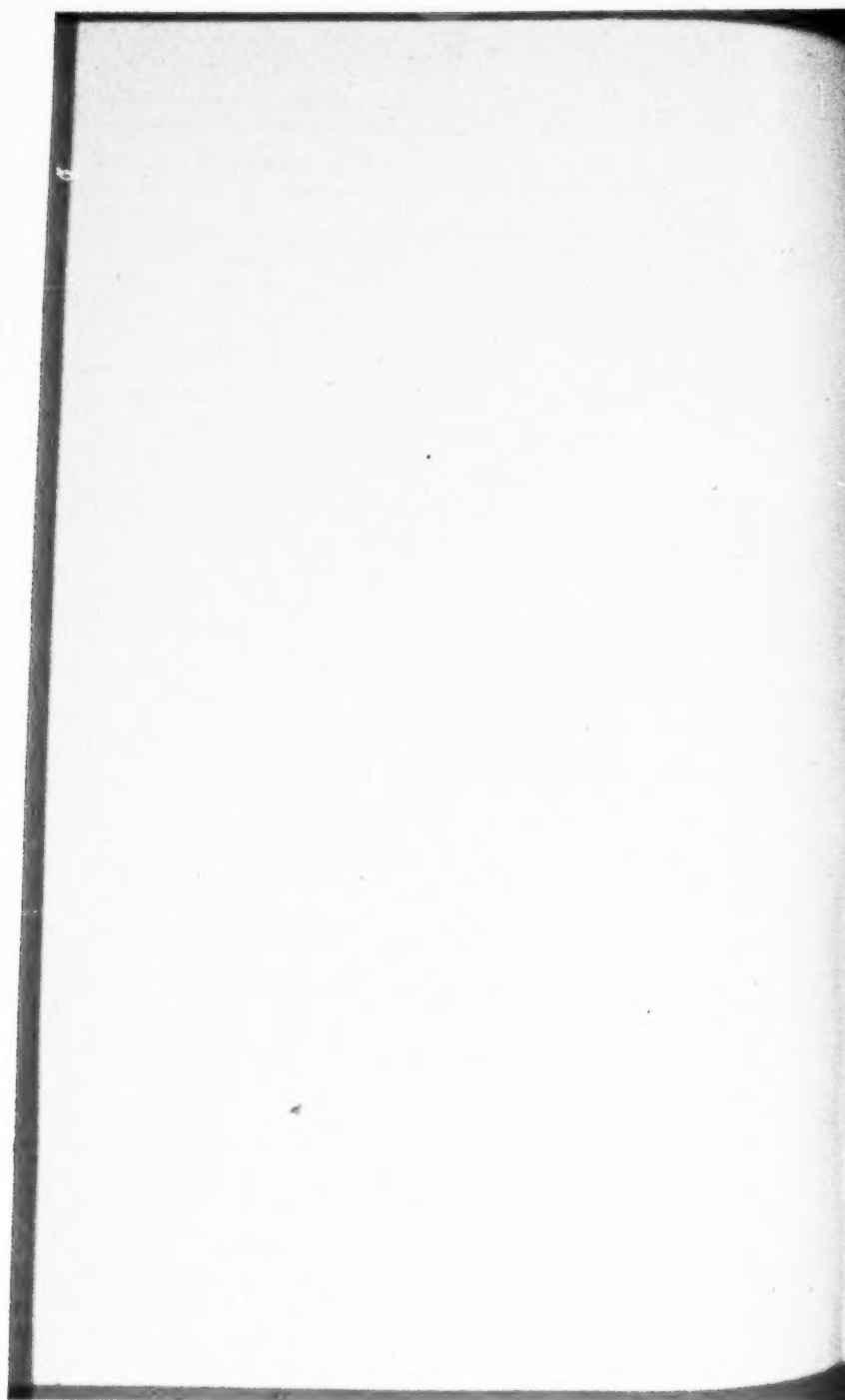
If it be true that appellant Pacific Improvement Co. has agreed to pay off and discharge this Lackawanna claim, said company being at the same time the owner of the claim, that extinguishes the claim and in no event can appellants hope to prevail in this case. These facts having come to light since the decision of this case in the courts below we knew of no way of getting that fact before this court as an answer to the merits. But for the purposes desired we have no doubt this court has the right to consider that fact and to examine the opinion of Circuit Court of Appeals and the record upon which it is based. And so we cite the court to the opinion and have filed with the clerk of this court for the use of this court and opposing counsel several copies of the printed record used in the Circuit Court of Appeals. And call attention to the depositions of Thos. H. Hubbard, Geo. E. Downs, ~~H. E. Gatos~~ and Wilbur F. Boyle copied in said record pages 489 to 505 and to the petition of Pacific Improvement Company to reserve fund in court, page 450 and 451 which show the facts very clearly that the Pacific Improvement Company the appellant here is the purchaser at the foreclosure sale and the decree in the record proper shows that the purchaser assumed the payment of that claim. (R. p. 40, 41.)

This brief reference to said case and record is sufficient to put this court upon notice of the facts as subsequently developed so as to shape its decree in case that should become necessary to give these appellees an opportunity to protect themselves against said claim.

Respectfully submitted,

L. W. CAMPBELL,

Solicitor for appellees, Moran Bros. and Henry K. McHarg.



N^o. 162. 22.

U.S. SUPREME COURT U.S.
FILED

MAR 4 1899

JAMES H. MCKENNEY,

Brief of Turner & Mott for Appellants
SUPREME COURT OF THE UNITED STATES,

OCTOBER TERM, 1898.

Filed Mar. 4, 1899.

NO 162.

THE LACKAWANNA IRON AND COAL COMPANY, *et al.*,
Intervenors and Appellants,

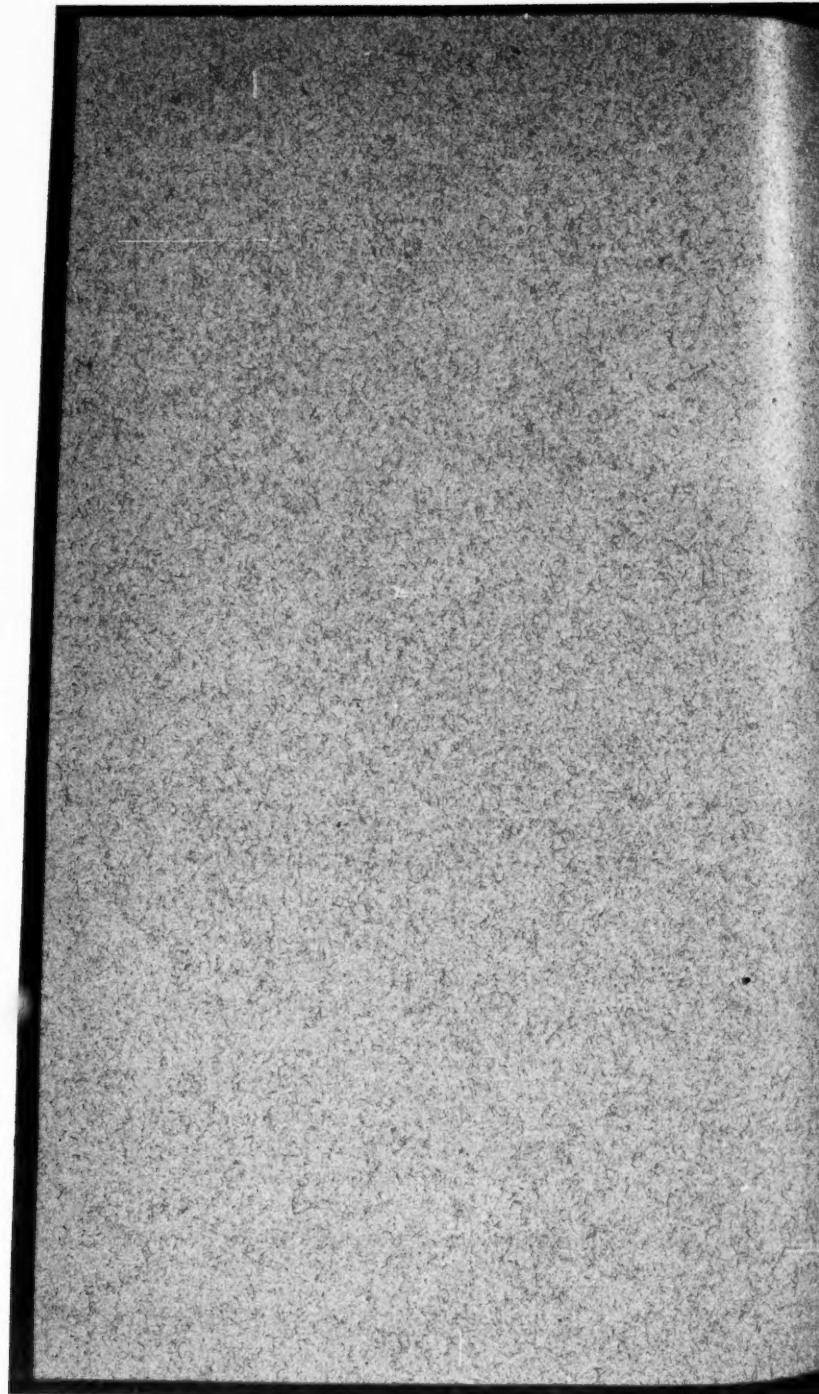
vs.

THE FARMERS' LOAN AND TRUST COMPANY,
Complainant-Respondent.

SUPPLEMENTAL BRIEF FOR THE FARMERS'
LOAN AND TRUST COMPANY.

HERBERT B. TURNER,
M. F. MOTT,

Solicitors and of Counsel for
THE FARMERS' LOAN AND TRUST COMPANY.



SUPREME COURT OF THE UNITED STATES,

OCTOBER TERM, 1898.

THE LACKAWANNA IRON AND COAL
COMPANY, *et al.*,
Intervenors and Appellants,

vs.

THE FARMERS' LOAN AND TRUST
COMPANY,
Complainant-Respondent.

No. 162.

Supplemental Brief for the Farmers' Loan and Trust Company, Respond- ent.

In view of the very elaborate Brief, of nearly one hundred pages, submitted by the Appellants, we will ask the Court to permit us to file this memorandum in reply.

The matter, as submitted to the Court by the appellants, is, unfortunately, largely complicated with the entire Houston and Texas Central litigation. Many facts are set up by them which hardly seem to us pertinent to the issues now before the Court. Indeed, the questions here are very simple, as the Court will see by examining our original brief filed in this cause.

The appellants state in the second paragraph on

page 2 of their brief, that default was made by the Railway Company on January 1st, 1885, in the payment of interest on its "First Mortgage Bonds." This fact was found by the Master (page 105 of the Record) in this form. But care must be taken to distinguish between the several classes of bonds referred to here as "First Mortgage Bonds." That description, as used by the Master, includes the First Mortgage Main Line bonds, amounting to \$6,262,000; the First Mortgage Western Division bonds amounting to \$2,270,000; and the *First Mortgage Waco and Northwestern Division* bonds amounting to only \$1,140,000. We are concerned solely with the last-mentioned bonds, the default on which, on January 1st, 1885, amounted to only \$39,900, the semi-annual interest due that day, out of a total of \$833,760 then defaulted by the Railway Company (Rec. p. 105). The Waco and Northwestern division was but a small portion—but $11\frac{1}{100}$ per cent.—of the Houston and Texas Central System—being only 58 miles long as against 520 miles for the whole system. This comparison should be remembered when considering the matters mentioned in the Appellants' Brief and the dealings of the Receivers, who were receiving and disbursing the moneys of the entire road and managing its general affairs regardless of its divisions. They did not even keep separate accounts for the divisions (Rec. p. 110), and it is impossible to tell, as the Master himself finds (Rec., p. 110) "what, if any, of the expenditures made by the Receivers in causes Nos. 185 and 198 for extraordinary repairs, betterments and improvements, and for operating and running expenses, were made for said Waco and Northwestern division, * * * and this is true also as to *receipts and incomes*."

Now, let us see what the situation was when, for the first time on January 1st, 1885, default was made in first mortgage coupons, including those due under the Waco and Northwestern Division mortgage. Before that date, it will be admitted, the holders of that mortgage had no power to take any action whatever with regard to the mortgaged property, nor indeed did the mortgage permit them to act until 60 days after demand, based on such default (Rec., p. 15). We wish to call the Court's attention to the events which had already become *fixed and settled facts* when the first default on our mortgage occurred, and during a period when we were helpless, by the terms of the mortgage itself, to control in any way the actions of the railway company.

- (a.) The three contracts for steel rails referred to in the petition had been made by the Railway Company with the Lackawanna Company on December 28th, 1882. April 26th, 1883, and October 30th, 1883, respectively (Rec., pp. 99-102). With the two first contracts and the rails delivered under them, we are not concerned. The petitioners abandon any claim as to them (Brief on behalf of Petitioners, p. 5). The only contract to be considered by the Court is that of October 30th, 1883, made *one year and two months* prior to any default in payment of interest.
- (b.) The period limited in this last mentioned contract for the delivery of the 10,000 tons of steel rails called for by it had expired, that period being between February 1st and August 1st, 1884 (Rec., p. 102).
- (c.) The total actual delivery of rails under this contract, amounting to 8,552 tons had been

made in the months of *February, March, April and May of 1884*, that is to say, such delivery had been completed and the last rail delivered *seven months* before any default in the payment of interest (Record, p. 102).

(d.) The time for the payment of the purchase price for all these rails—which, under the contract was to be made either *in cash on delivery* or in *six months'* notes of the railway company dating from the average date of *delivery*, with a privilege in the Railway Company to renew such notes before their maturity for a further term of *six months*—had matured in the following manner: The company had given notes instead of cash for all the rails, which, if made in accordance with the contract and collected when due instead of being extended, would all have matured finally by the first day of December, 1884 (Rec. pp. 102, 103). But the Lackawanna Company “for the accommodation and to suit the convenience” of the Railway Company, had voluntarily given the latter in the contract the privilege of extending the notes, so that the last of them *as so extended* did not fall due until May 18th, 1885 (Rec. pp. 103). The amount of the notes due at this date (May 18th, 1885) was \$327,175.50—being the *total* balance of principal due for the rails delivered under the contract with which we are concerned (Rec., p. 103). Of this amount, only \$99,300.64 is claimed by the appellant to have gone into the Waco and Northwestern Division, that division, as has already been pointed out, being only 58 miles out of a total of 520 miles for the whole system, and of those 58 miles only 30.8 being laid with the

rails in question (Rec., p. 104, and Petitioner's Brief, pp. 5-6).

- (e.) All the rails delivered to the Railway Company by the appellants had been placed in the Railway Company's tracks immediately on delivery and, therefore, long before any receivership or default on the Waco and Northwestern Division Mortgage (Rec. p. 105).

In view of these facts, what becomes of the appellants' argument, based on the theory that the appellee's alleged delay in *taking possession* had constituted the Railway Company its *agent* to operate the road and to make expenditures for its protection, including this expenditure for steel rails, with the understanding that such expenditures would create a first lien on the property, prior to the mortgage? This argument runs all through their brief, in the Statement of Facts as well as in the Points of Law. On page 22 we find the proposition that "the mortgagee, by leaving the mortgagor in charge of the mortgaged property, makes him his agent to create any lien necessary and proper to save and preserve the property and keep it a 'going concern.'" On page 39 we find the proposition that "the mortgage creditors, by leaving the railway company in possession of the property, impliedly authorized it to create any liens thereon which might be necessary to keep up the property, and enable it to continue to earn the interest upon the mortgaged debt." The discussion of this proposition extends from page 39 to page 48, and a number of authorities are cited which, as we shall point out, do not even sustain that proposition as a naked theorem. The italics on pages 50, 53, 54, 56 and 57 are

all inserted with a view to supporting the same argument, and a very important part of the appellants' contention will be destroyed by showing (1) the fallacy of the argument itself, and (2) its inapplicability to this case even if it were otherwise valid.

Before discussing these two points, however, we will add a few words as to another argument in this connection which, it begins to dawn on us, is now being urged by the appellants. We mean the argument that a trustee, *by the very act of accepting* a Railroad trust-deed, and not taking possession of the railroad immediately *upon the execution* of the instrument, is thereby to be considered as authorizing the railroad company to act as its *agent* and to create liens superior to the mortgage for whatever expenditures may be deemed *necessary* to the preservation of the property! In other words, it is now argued that the mortgage is not the first lien it purports to be because the trustee did not do something which by the terms of the mortgage itself, and in the nature of things, it could not do—namely, take possession of the property and run the railroad at once.

The First and Second Points (Brief, pages 20 to 48) show clearly that this theory is in the minds of appellants' counsel. Yet we feel safe in saying that no such extraordinary doctrine has ever before been advanced in a railroad mortgage case. From the number of instances of *chattel mortgages* cited by the appellants, we should infer that their doctrine is designed as an extension of certain propositions concerning *individual chattel mortgages* with or without possession which they assume to be law. And this inference is strengthened by the remarks on page 48 of the appellants' brief, in which they seek to show that there is no difference in the rules

applicable to ordinary individual mortgages on specific things, and those applicable to mortgages upon vast systems of corporate property. But, assuming that the propositions advanced by the appellants were true as regards private mortgages (which we very much doubt), they themselves point out, on the same page, that this Court has declared railroad mortgages to be "peculiar in their character" (*Fosdick vs. Schall*, 99 U. S., 235.) They point out at the same place that this Court has refused to apply the principles which govern in railroad cases even to cases of other *corporate* enterprises (*Wood vs. Guarantee Trust Co.*, 128 U. S., 416, 421.) They say that railroad mortgages are not *sui generis*. But this Court has said that they are, and, in the nature of things, they must be.

"There is a broad distinction" said this Court in the *Wood* case, above cited, "between such a case and that of a purely private concern." And the Court, in that decision, was declining to extend the doctrine of *Fosdick vs. Schall*, to cases other than railroad cases, thus showing that one of the important distinctions between private mortgages and railroad mortgages lies in the very matter now before the Court.

In *Shaw vs. Railroad Co.*, (100 U. S., 613,) this Court said distinctly: "Railroad mortgages are a peculiar class of securities."

But it would seem unnecessary to remind the Court further of its allusions to this manifest fact. To argue that unless the trustee takes possession immediately on the making of the mortgage its lien is liable to be divested by the railway company acting as its agent in certain respects is to make a different contract from that which the mortgage makes. The *mortgage* expressly preserves the railroad company from all interference by the trustee as long as the interest is paid.

For what object is a railroad company organized if not to operate its railroad? Did anybody ever hear of a Trust Company's taking hold of a railroad as soon as the mortgage was made and operating the road while the railroad did nothing? It is a matter of common knowledge that in most instances one of the first acts of a railroad company after organization is to issue bonds and to make a mortgage securing them. The reason is obvious. Such bonds are necessary to fund the enterprise and, generally, to build the railroad. What folly, then, to suppose that a case could ever arise where a railroad trustee might, *under the terms of the mortgage*, take instant possession of the property and thus deprive the railroad company of the one purpose for which it came into existence! This reflection shows the cardinal distinction between railroad and private mortgages. And, since it is inconceivable that the trustee should ever take possession *instantly under the mortgage*, the proposition of the appellants, if it means anything, must mean that Railroad Companies *are not able*—that is, are not permitted by law—to make first mortgages which they may not afterwards displace by means of new liens. It is said that these new liens must be for *necessary* expenditures. But who shall determine what are *necessary* expenditures? Perhaps, in order to keep the road a “going concern” it would be *necessary* to make another mortgage, and, in that case, according to the appellants' argument, the *second* mortgage would be the *first* lien! This, indeed, is the proposition towards which the appellants gravitate—a proposition known to no law except the law of admiralty where the latest service is held entitled to the first lien.

The appellants cite a number of *admiralty* cases

where this doctrine is undoubtedly applied. But this Court has held over and over again, on such applications as the present, that the cited doctrine of admiralty law does not apply to railroads. (*Galveston vs. Cowdrey*, 11 Wall., 459, 482; *Thompson vs. Valley R. R. Co.*, 132 U. S., 68; *Fogg vs. Blair*, 133 U. S., 534; *Toledo R. R. Co. vs. Hamilton*, 134 U. S., 296. And see also the able opinion of Judge Manning in *Meyer vs. Johnston*, 53 Ala., 237).

But perhaps we mis-read the appellants' argument, and perhaps they intend after all only to contend, as has so often been done in this class of cases, that the claims of the Lackawanna Company were in some way improved as against the bondholders by the trustee's failure to take possession or to bring suit immediately upon the maturing of its right to do so under the terms of the mortgage. As already pointed out, that right matured sixty days after demand based upon the default of January 1st, 1885. We will, therefore, consider this argument under the two heads already indicated on page 5 of this brief :

1.—The argument is fallacious in itself.

This subject has been shortly discussed in our original brief (pages 26-28). But in view of the reliance which the appellants seem to place upon this phase of the case, we will here expand a little the ideas suggested there.

In some of this Court's decisions on the so-called "back-claims," expressions are found calling attention to the delay of mortgagees to take possession, and intimating that such delay may be an element in a general situation *estopping* the mortgagees from insisting on the pri-

ority of their lien. Some of these expressions are quoted by the appellants (Brief, pages 50, 53, 56, and 57). But a reference to those cases will show that they have no such effect as is attributed to them ; that the matter of delay in taking possession was only a minor element in the numerous elements of decision ; that in so far as it was an element at all, the Court's argument was largely a corollary of the undisputed principle that railroad mortgages cover only *beneficial* income after deducting *current operating expenses* (the Master has emphatically held that the appellants' claim is not a current operating expense, Rec., p. 104) ; and that the logic of the Court ran thus : The trustees could, if they saw fit, be in possession ; if they were in possession, their lien would only attach to *beneficial* earnings after the payment of operating expenses ; such operating expenses would necessarily be incurred in keeping the road a going concern ; it is reasonable to assume, under such circumstance, a consent on their part to the incurring by the railroad of operating expenses, payable out of the earnings ; and, therefore, when the earnings have been applied, not to the payment of these expenses, but for the benefit of bondholders, it is equitable to require a restoration of them out of the receivership income. The meaning of this is readily perceived. Clearly, it does not rest upon any doctrine of implied *agency*. The extent of the claims to be allowed, the limit of time during which they may be incurred, and the conditions under which an implied consent can be raised from delay, must necessarily depend upon the peculiar circumstances of each case. The *sine qua non* is that the *claims* should be ordinary operating expenses ; that they should have arisen *after* the trustees were in a position to take or demand possession ; and that earnings which the *railroad company* should have applied to the payment of the claims

were, during the period of the trustees' neglect, paid to or for the benefit of the bondholders.

These principles are made clear by the decisions of this Court cited by the appellants. Take, for instance, the *Morrison* case, quoted by them on pages 50-51 of their brief. In that case, the default having taken place in October, 1873, and the trustees having neglected to take possession, over a year later one Morrison went as surety on a bond for the Railroad Company to stay the execution of a judgment against it. In 1877, the Court decided against the Railroad Company on the bond and the surety became liable. Not until after all this had happened did the trustees see fit to institute foreclosure proceedings. Thus, Morrison's claim against the railroad company for indemnity because of his liability as surety on its behalf, had arisen and matured *during* the open neglect of the trustees to enforce an already existing default. And it was with reference to that neglect that this Court used the language quoted by the appellants. The crucial point was that the trustees, being in a position to seize the property, wilfully "allowed the railroad company to continue to use the property, and to take care of it for them, and stood by and saw Morrison (who had no interest in the matter) put his hands into the fire and rescue the rolling stock of which they were to receive the benefit." But even this would probably not have been sufficient to sway the decision in favor of Morrison, but for a multitude of other circumstances, all of which the Court considered in a very long opinion, calling the case "a special one."

Burnham vs. Bowen, (111 U. S., 776,) also quoted by the appellants at page 53 of their brief, proceeds on precisely the same grounds. In that case the mortgage having been made in 1871, no interest was ever paid, and the trustees might then and

there have taken possession. Instead of doing so, they allowed the Railroad Company to continue in possession for over four years. *During this period of neglect* Bowen furnished coal to the Railroad Company, which failed to pay for it, and applied all the current income to improving the bondholders' lien by paying off prior encumbrances on the property. Under these circumstances, this Court authorized the payment of Bowen's coal bill prior to the bonds. His claim was a current operating expense. It arose and matured during the trustee's neglect. The current earnings concededly applicable to the payment of such expenses were used for the benefit of the mortgagee.

"We do not now hold," said the Court, "any more than we did in *Fosdick vs. Schall*, or *Huidekoper vs. Locomotive Works*, 99 U. S., 258, 260, that the income of a railroad in the hands of a Receiver, for the benefit of mortgage creditors who have a lien upon it under their mortgage, can be taken away from them and used to pay the general creditors of the road. *All we then decided, and all we now decide, is, that if current earnings are used for the benefit of mortgage creditors before current expenses are paid, the mortgage security is chargeable in equity with the restoration of the fund which has been thus improperly applied to their use.*"

In *Union Trust Co. vs. Souther*, (107 U. S., 591,) quoted by the appellants on pages 56 and 57 of their brief, the same principles governed the Court's decision. In that case, besides the elements existing in the cases already cited, there was an actual express *consent* on the part of the trustee from which an estoppel against it in favor of the claimant could readily be deduced. Default had been made as early as 1873. The complainant's bill was not filed until 1877. The Court had made an order requiring the Receiver, after paying current expenses, etc., to pay labor and supply

debts that accrued within the six preceding months. During the receivership the net earnings exceeded \$200,000. The whole amount, under the orders of the Court, *and with the consent of the complainant*, was from time to time expended in purchasing additional rolling stock, etc., and making permanent improvements, instead of discharging the claims under the six months' rule aforesaid. The property so acquired was sold with the rest under the mortgage, and the sale left a balance of mortgage debt unsatisfied. The intervenor had proved a claim under the six months' rule for \$500, and he claimed payment of this claim out of the proceeds of the sale. It seems a plain case. The claim was sustained of course. In a long opinion reviewing all the facts and many authorities the Court used the language quoted by the appellants. The meaning of that language in view of the above facts is very evident and further illustrates the principles which govern in such cases, as we have set them forth in this brief. Nothing could be clearer than that there was no intention on the part of the Court in those cases to establish a doctrine that by a delay in taking possession after default the trustee makes the railroad company or anybody else its *agent* to incur debts.

No such interpretation can be placed on the language of the Court.

In the *Matter of the Dexterville M'f'g & Boom Co. vs. Case* (4 Fed. Rep., 873), an attempt was made to obtain a preference for a claim of damages to property by fire from a locomotive. After citing *Hale vs. Frost*, the Court said:

"To sustain the claims in question, it is, therefore, necessary that some equity be found in favor of the petitioners, and superior to that of the bondholders upon which to base their allowance. And the supposed equity urged is that the

fire in question occurred after default on the part of the railroad company in payment of the mortgage debt or interest ; that thereafter the company operated the road as the agent or trustee in equity of the bondholders, and that the alleged liability sought to be enforced in the present proceeding arose from such operation of the road and as an incident thereto ; that, therefore, it may be put under the head of operating expenses. * * * No relation of principal and agent, either in law or equity, can be implied from the mere fact that the railroad company continued to operate the road after it was in default in payment of the mortgage debt, nor from the further fact that the bondholders did not take possession of the property after such default, nor from both facts combined. * * The negligence of the company, if there was negligence at all, occasioned the loss. For that negligence it alone was responsible. To sustain the position taken by the petitioners, it must be held that the bondholders at least impliedly assumed liability for the negligence of the railroad company. * * * I cannot so hold. * * * In no just or proper sense could such claims as these be considered as part of the operating expenses upon which the petitioners could assert a right prior to that of the mortgagees. They are wholly unlike claims for supplies, new equipment, right of way, and new construction, or any claim falling legitimately under the head of operating expenses. * * * It is not improper to add that this ruling is supported by the practice of the learned Circuit Judge of this circuit." (Seventh Circuit.)

In *Blair vs. St. Louis H. & K. Co.* (22 Fed. Rep., 471), Mr. Justice BREWER made the following significant remarks :

"What claims are entitled to such equitable preference? The master has reported in favor of all claims accruing since the default in payment of the interest on the mortgage debt—a period of over two years. This seems to proceed upon the assumption that the mortgagees, by failing to take action, have made the mortgagor company their agent to incur debts ; have impliedly consented

that all such debts should take preference of their secured claims. I do not think that this principle is sound. There is no implied agency to that extent, and I do not think that the rulings of the Supreme Court are based upon any such doctrine. The idea which underlies them I take to be this: that the management of a large business, like that of a railroad company, cannot be conducted on a cash basis. Temporary credit, in the nature of things, is indispensable. Its employees cannot be paid every month. It cannot settle with other roads its traffic balances at the close of every day. Time to adjust and settle these various matters is indispensable; because, in the nature of things, this is so, such temporary credits must be taken as assented to by the mortgagees, because both the mortgagees and the public are interested in keeping up the road, and having it preserved as a going concern, and whatever is necessary to accomplish this result must be taken as assented to by the mortgagees. In this view, such temporary credits accruing prior to the appointment of the Receiver must be recognized by the mortgagees, and such claims preferred. Now, for what time prior to the appointment of a Receiver may these credits be sustained? There is no arbitrary time prescribed, and it should be only such reasonable time as, in the nature of things and in the ordinary course of business, would be sufficient to have such claims settled and paid."

In the same case, upon another intervention (22 Fed. Rep., 769), TREAT, J., referring to the opinion of Judge Brewer, said:

"In this case, Judge Brewer, reviewing the authorities, cursorily intimated that demands which had accrued within six months prior to the appointment of a receiver, if they pertained to betterments, or the current necessary operations of the road, should be considered as equitable demands prior in right to the mortgage. There are two propositions underlying the rulings of the Courts: *First*, When, under the conditions of a mortgage, the mortgagee, after default, permits the corporation to still operate the road, the operations

thereafter must be considered for the benefit of the mortgagee and all others in interest, especially if betterments accrue therefrom. *Second*, To prevent the indefinite extension of such claims, the Courts limit the time within which such demands may be pursued * * *

"The mortgagee could have taken possession of the road under default, had he so elected. He preferred that the corporation should still continue to operate the road, certainly as much for his benefit as that of other parties. Why, then, as after-acquired property is to be included within his mortgage, should he not deal with said betterments according to equitable rules? True, there should be, as stated by Judge Brewer, some limit to the enforcement of such alleged obligations—fixed in this case at six months."

On a motion for a re-hearing of the above intervention (23 Fed. Rep., 704), Judge BREWER was again called upon to discuss this question. He said :

"Some criticism was made in the argument on what was said by brother Treat as to the mortgagor being agent of the mortgagee after default in the payment of interest. I do not think my brother Treat meant to be understood as laying down as a general proposition that wherever there was default the mortgagor became the general agent for the mortgagee for the contraction of debt. Certainly, if he did, I should not feel like agreeing with that view."

In the case of *Dow vs. Railroad Company* (20 Fed. Rep., 260), Judge CALDWELL had used the following argument to sustain a sweeping order appointing a Receiver :

"The first clause is proper, because it has been opened to the plaintiffs to apply for and obtain the relief they now seek, for more than a year, and by permitting the company to run and operate the road, they must, as between them and the persons furnishing labor, supplies and materials for the use of the road, and those damaged by its operation

be held to have impliedly assented that the earnings of the road should be applied to pay such expenses and liabilities which, in a greater or less degree, were incurred for the plaintiffs' benefit."

Commenting on this argument, Judge JENKINS in the case of the *Farmers' Loan and Trust Co. vs. Green Bay, W. & St. P. Ry. Co.* (45 Fed. Rep., 664), said :

"A careful reading of all decisions of the supreme tribunal upon that subject convinces me that Judge Caldwell has either misconceived the underlying principle of these decisions, or seeks to extend it unduly.

"The Supreme Court, as I read the opinions, has been most careful to limit the doctrine to claims representing that which has inured to the benefit of the mortgaged property, such as labor and supply claims, amounts due to connecting roads for materials, repairs, ticket and freight balances, and the like, allowing priority to such claims, because their non-payment would cause cessation of work, supplies, and running arrangements, and result in stoppage in the operation of the road, which, in the interest, as well of the bondholder as of the public, is not to be tolerated. * * * * *

If failure to take possession works an implied assent that the earnings should be applied in compensation of casualties in priority to the mortgage, why not as to all floating indebtedness, to all improvements upon the road, and irrespective of time? Why not say that, through failure to take possession, the bondholders assent that earnings should be devoted to the payment of all debts incurred after default in the payment of interest, and in priority thereto? Why limit such priority to the period of six months prior to the receivership? If priority is to be predicated upon implied assent instead of upon benefit to the *res*, it should be allowed to all claims arising during failure to take possession from which assent is implied. The priority should be co-extensive in point of time with the implied assent. That logically results from the principle bottomed upon implied assent. Such doctrine is, to my thinking, a broad

departure from the equitable doctrine declared by the Supreme Court, and would be ruinous in its consequences. If conceded, the entire floating debt of a railway company, occurring after default in payment of interest, and during failure to take possession, would necessarily and logically be given priority. Vested rights of property would be subjected to great detriment under such holding. The bonds of American railways are scattered throughout Europe, and are held in many hands. It requires much time to institute concerted action by the holders after default in payment of interest. Meantime, unprincipled directors, anxious to retain possession of the road, could contract indebtedness—given priority by such ruling—working ruin to the mortgage interest. The bondholder would be ‘improved out of his estate,’ and his vested rights placed at the mercy of hostile directors. I am unwilling to assent to such doctrine. I do not understand it to be the law. The rule is that current income should be first devoted to the current expenses of operation. Liability for death is not an expense of operation in any just sense of the term. It is an unsecured debt, and as such, cannot take precedence in payment over prior and express liens. *St. Louis, etc., R. R. Co. vs. Cleveland, etc., Ry. Co.*, 125 U. S. 658, 673, 8 Sup. Ct. Rep., 1011.”

This strong opinion shows the care which Courts should exercise in spelling out an estoppel from the acts of bondholders. Consent can only be implied where the reason of the case requires it. Ancient claims do not acquire a right to priority simply because they arose after a default in payment of bonded indebtedness. Delay in taking possession after default may, under some circumstances, become an element in estopping mortgagees from claiming their prior lien, but it cannot be made use of to resuscitate old claims, to load the property with burdens, and to relieve claimants from the consequence of their own neglect to collect their claims from the railroad company within a reasonable period.

"It has never been decided yet that because a mortgagee does not immediately pounce upon his security, foreclose, take possession, and sell, that he impairs the obligation of his lien."

*The Atlantic, Mississippi & Ohio
Case (3 Hughes, 340).*

In the case of *Coe vs. New Jersey Midland Ry. Co.* (31 N. J. Eq., 105), the highest Court of New Jersey reviewed these questions. An attempt was made to prefer labor claims over the mortgage debt, it being asserted that the services of the laborers were of great value in preserving the mortgage security, etc., and it being made to appear that after default in payment of interest, the mortgage trustee allowed the mortgagor company to continue in possession and operate the road, instead of taking possession, as he might have done under the mortgage. The Court held that the fact that the employees were not aware when they rendered their services that default had taken place, gave them no claim against the mortgagees for their wages, notwithstanding an Act of the Legislature which provided that whenever the Chancellor should appoint a Receiver of any railroad, the Receiver should apply all incumbered personal effects and all moneys which might be transferred to him at the time of assuming his duties to the payment of wages then due to employees of the company for not over two months back. The Court said that the lien which this act gave could not be extended so as to impair the obligation of lien of duly recorded incumbrances antecedent to the act. The *Galveston R. R.* case was cited in support, and *Fosdick vs. Schall*, was distinguished. The Court further says :

"The mortgagees owed to the employees of the mortgagor no duty under the circumstances; they were at liberty to refrain from taking possession if

and as they saw fit, and by so doing they incurred no liability to the employees of the mortgagor to indemnify them on the contracts, express or implied, of the latter with them for the payment of their wages. The mortgages were on record, and the record was notice to all. It surely would not be claimed that the holder of a mortgage past due upon a farm is liable, merely because he is a mortgagee, for the wages of the hands employed by the mortgagor in working the farm after default, * * * although it may have been of the greatest importance to the mortgagee's security that the farm * * * should not go untilled. It is due to the proper administration of justice that the rights of all parties shall be clearly understood and strictly respected, and recourse is not to be had to devices, either by way of refinement in the application of principles or the introduction of new doctrines to effect purposes which, however commendable in their design, result in operation in taking the property of one man to pay another's debt, and in creating liens in favor of one class of creditors to overrule the existing lawful liens of others, which is neither according to law or equity, and is in violation of constitutional rights. * * * Such liens could not be confined to that class of meritorious creditors, but must be extended to all others with claims equally meritorious, though not for the wages of labor."

Even, then, had there been any delay after default such as is asserted by the appellants, and the appellants' claim had arisen *during* this delay (which is not the case), the above authorities show that no *agency* would have been created by that delay, that many other circumstances, would have had to be considered to create an estoppel against the mortgagee, and that, the appellants' claim not being an *operating* expense, no consent to its creation could have been implied against the mortgagee.

(2.) Whatever the argument to be

deduced from delay in taking possession, that argument is inapplicable here, where there has been no delay.

We have already on pages 3-4 of this brief stated the facts showing that the appellants' claim, declared by the master not to be in any sense a current operating expense, arose and matured, was extended voluntarily by the appellants, and, as so extended, again matured for the most part, before any default occurred on any of the Railroad Company's bonds, before the rights of any of the mortgagees to take possession sprang into existence, and before any *valid* receivership was created. Indeed, since even the receivership, created under the Southern Development Company's bill and afterwards declared void, only began on February 21st, 1885 (Rec., p. 106), these things had nearly all happened before the inception of that receivership. What justification, then, is there for all this talk of delay? If it were true, as appellants assert, that the trustee of the Waco and Northwestern Division mortgage slept on its rights from March, 1888, the date when its rights arose, to April, 1889, the date when its foreclosure bill was filed, how could that in any way improve the claim of appellants, whose lien, if they have any, necessarily matured *before* the beginning of the trustee's alleged supineness and at a time when it had no power to act, and, indeed, no knowledge of the situation? It must not be forgotten that at the time when the rails were delivered (February to May, 1884), and when, therefore, if ever, the appellants' lien must have arisen, the Houston and Texas Central Railway Company was a solvent, going concern, with the best of credit, as is shown by the fact that it could make such contracts as the three made with these very appel-

lants, and it was operating its various lines of railway, including the Waco and Northwestern Division, and paying its debts and obligations as they matured, including the notes and obligations given for the rails under the prior contracts as they matured from time to time. Moreover, there was no default in the payment of any mortgage interest.

This being the very excellent condition of affairs of the Houston and Texas Central, so far as the world knew and so far as its bondholders knew, in 1884, the bondholders had no right to make any inquiry as to the way in which the road was being run. They could not ask what contracts were being made for rails or for anything else. They were receiving what they were entitled to, and that was their interest, and they had no right to ask for anything else, and it was nearly a year after May, 1884, when the last rail was delivered, before the road went into the hands of Receivers, and it was two full years before the road passed into the hands of a Receiver legally and properly appointed.

But was the trustee supine even after its rights accrued, on March 1st, 1885? The receivership under the Southern Development Company's bill, begun on February 21st, 1885, fell like a thunderbolt out of a clear sky. The Farmers' Loan and Trust Company was not made a party to that bill. But on March 31st, 1885—*within 30 days after its right to act had matured*—that Trust Company filed its petition in the Southern Development Company's case, praying to be made a party for the protection of the several mortgages represented by it (Rec. p. 115). This petition was granted, and on June 15th of the same year the Trust Company filed its answer to the original bill and to a supplemental bill which had been filed in the meantime (Rec., p. 115). Presently, on May 27th, 1886, the Southern Development Company's bill

was dismissed and the receivership thereunder discharged, a new receivership being simultaneously created in a new cause, known as consolidated cause No. 198, in which the trustees of the main line mortgages *and the appellee*, as trustee of several mortgages, including the Waco Division mortgage, were named as complainants (Rec., pp. 108, 166). In this cause, the appellee filed an answer to the bill of the main line mortgagees, setting up its rights and praying for the payment by the Receivers of its overdue coupons (Rec., p. 117). The result was that on May 27th, 1887, an order was entered directing the Receivers to pay the two coupons on the Waco and Northwestern Division mortgage which fell due in January and July, 1885 (Rec., p. 117), and those coupons, with interest, amounting altogether to \$91,371, were accordingly paid (Rec., pp. 114, 117). The appellee also filed petitions for the payment of subsequent coupons but no orders were entered on those petitions (Rec., p. 117) and finally it filed its bill to foreclose the Waco and Northwestern Division mortgage in April, 1889.

How, under these circumstances, can it be said that the appellee was dilatory in protecting its interests? The property came into the hands of the Court before the appellee's right to act matured; within a month of that right's maturing, appellee moved the Court to admit it as a party to protect its interests; it knew that the property was safe in the hands of the Court under one receivership or another without a break until it should file its own foreclosure bill; it was at all times before the Court presenting its views as to the administration of the property and seeking, and sometimes obtaining, payments on account of its debt; and it knew that by filing its own foreclosure bill during the pendency of the prior bills no additional pro-

tection would be gained to that which existed already. To say that it was neglectful of its rights under such conditions is simply to fly in the face of facts.

(3.) The appellants have no lien upon either the earnings or the corpus.

In the first place, the appellants claim (Brief, p. 20) that when the contract was made with the Houston and Texas Central Railway Company, by which they sold, and the Railway Company bought, certain rails, a *lien* was created upon the income and the *corpus* of the property superior to that of the mortgage creditors.

Lest we should misapprehend their position, they again, on page 48, state their claim that the furnishing of the rails created a lien in favor of the Lackawanna Company against the Railway Company and its property and the income thereof, and that such lien is superior to the mortgage, upon the ground that the mortgage creditors impliedly authorized the Railway to create such a lien and have received the benefit of the rails.

Now, we have already pointed out the futility of that claim. But there are still other reasons which show the incorrectness of the appellants' position.

This *lien* which they are supposed to have created upon the Waco and Northwestern Division of the Houston and Texas Central was a lien upon a Texas railroad, with all its property in the State of Texas, forming a division of a great railway, the Houston and Texas Central, not one foot of which was outside of the State of Texas. Surely, if any contractors were ever amenable to Texas law, it would be those who were endeavoring to create and who did create, if the appellants are correct, a lien upon

Texas real estate, owned by a Texas corporation. If these parties had been making a written indenture of mortgage, no possible question could arise but that they were subject in respect to such mortgage to Texas law, and whether counsel call the lien, which they claim to have created, a legal lien or an equitable lien, or any other kind of a lien, it must, if a lien at all, be governed by Texas law.

Now, unfortunately for this entire lien doctrine, the statutes of Texas are peremptory on the subject.

The Act of 1876, as given in Sayles' Texas Civil Statutes and referring to railroad corporations, prescribes as follows :

"Art. 4220. No mortgage by such corporation shall be valid unless authorized by a resolution adopted by a vote of two-thirds of all the stock of such company, after notice and in the manner provided in this title for increasing the capital stock of such corporation.

"Art. 4221. When any such resolution has been adopted, in the manner provided in the preceding article, it shall be recorded in the office of the Secretary of State, and no such resolution shall take effect until so recorded."

If the appellants had any right to a lien under the statutes of Texas, they should have complied with those statutes. Failing to do so, they cannot escape from the consequence of their failure by claiming an equitable lien under the authority of *Fosdick vs. Schall*.

Farmers' Loan and Trust Co. vs. Chandler (18 S. E., 540).

But counsel will probably say that, after all, we are playing with words ; that he quite agrees with the Courts which have so frequently stated in these railroad cases that the equity which they allow is

not a lien, but, as Judge Drummond said in the 8th Bissell, 315, that in point of fact the allowance of these "back-claims" cannot be justly called a lien, but an exercise of equitable power in the premises. If this be so and if counsel takes that position, then surely the appellants had no *lien* when they advanced the rails, and the contention is not true (Brief, p. 45) that *the furnishing of the rails* created a *lien*. If there was no *lien*, then the appellants must take their position as ordinary intervening creditors, claiming on certain equitable grounds, a right to prior payment out of the property in the hands of the Court. We think that we have already shown that they have no such claim in equity. Counsel will find it very difficult to bring forward even a case of a private individual's mortgage where a party has been allowed to establish a lien by his labor or material furnished upon a piece of property when the mortgagee was ignorant of the fact that such labor or material had been furnished. In the present case the holders of these bonds and their trustee knew nothing about the fact that this railroad needed new rails, or that the Lackawanna Company had furnished those rails on credit. All they knew was that the interest was being promptly paid, and that the Railway Company was fulfilling all its obligations to those from whom it had borrowed money.

(4.) The Appellee's mortgage extended to and covered income.

On page 76 of their brief, the appellants assert that the Waco and Northwestern Division mortgage did not cover income. The mortgage shows the contrary. In the form of bond set forth in the mortgage (Rec., p. 13), and in the description of the property in the conveying clause (Rec., p. 14),

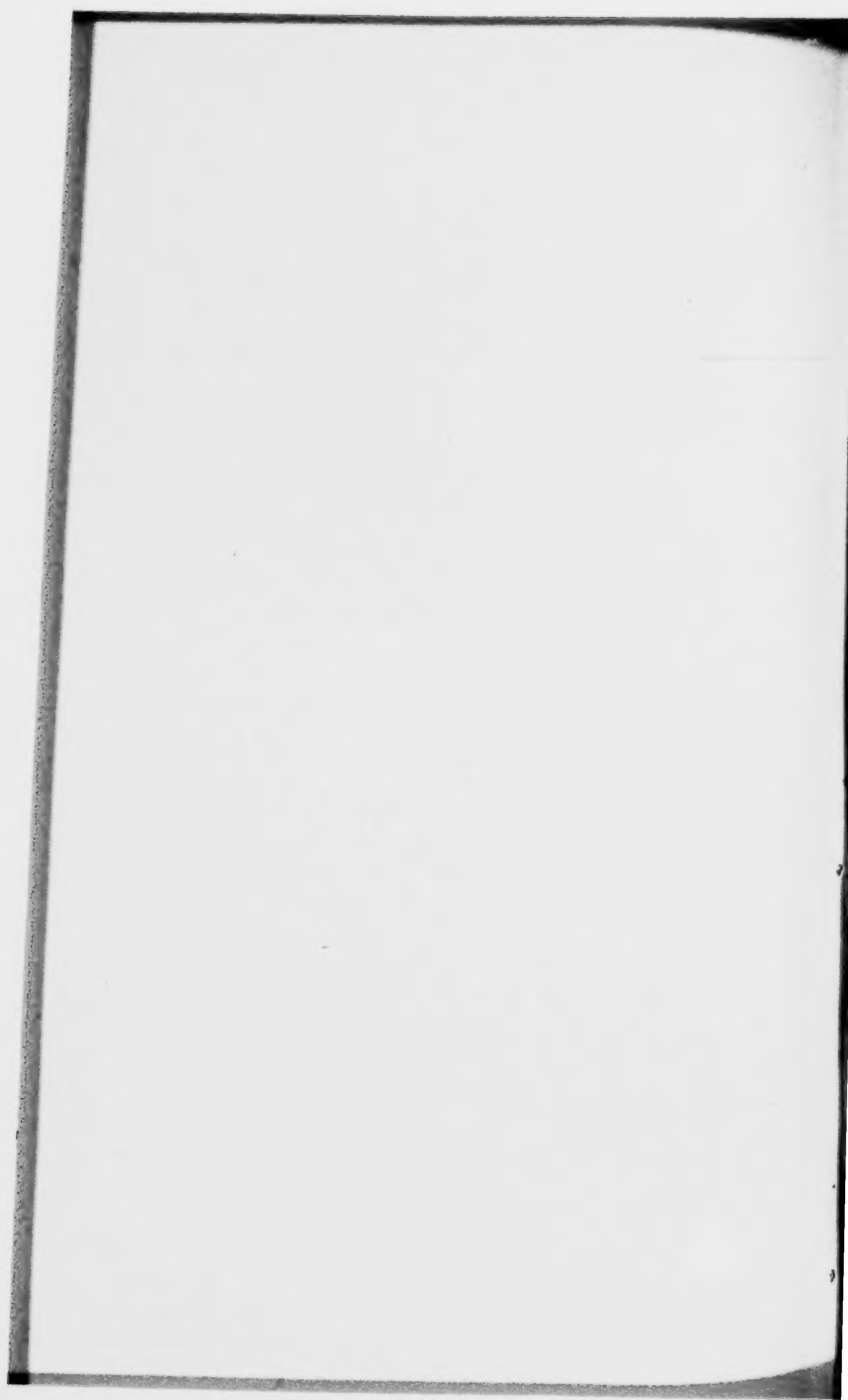
the language is clearly broad enough to include income. And the language of the provisions of the mortgage as to the trustees taking possession (Rec., p. 15) expressly mentions income and shows conclusively that it was the intention of the parties to mortgage the incomes.

But the appellants, seeking by an illogical argument, to sustain their *own* lien on the earnings by proving *ours* to be bad, say that whether income is covered or not, the trustee acquired no claim to it because it never demanded possession of the railroad company. And they cite the familiar cases establishing the doctrine that only the beneficial income is covered by such mortgages and that, before the income can be applied to the use of the mortgagee, it must be sequestered. But those cases did not require, as appellant seems to suppose, the institution of a foreclosure suit, or the actual taking possession by the trustee. Of what use would it have been to demand possession of the railroad company which had no possession after February, 1885, at which time the Court itself took possession of the road and sequestered its income under a general creditor's bill. We have already pointed out that as early as March, 1885, the appellee intervened and set up its claims against the property, and, without again going over the facts, we think it clear that from that time on the appellee kept its claims as mortgagee actively before the Court without interruption.

New York, March, 1899.

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The Farmers' Loan & Trust Company.



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FILED

MAR 8 1899

JAMES W. MCKENNEY

Ch. No. 22

Sup. Dy. of Campbell for Resp.
(16,664.)

Filed Mar. 8, 1899.
Supreme Court of the United States.

OCTOBER TERM, 1898.

No. 162.

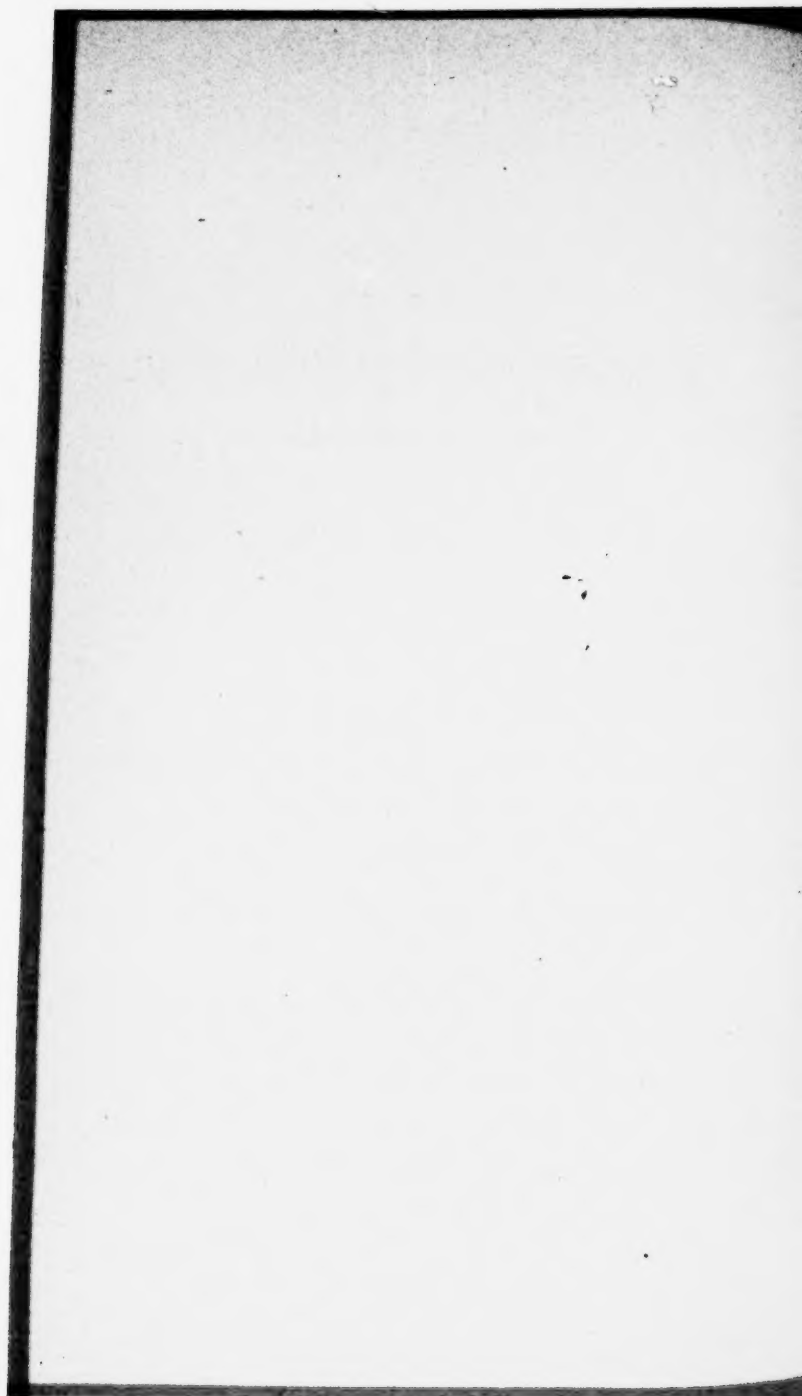
**THE LACKAWANNA IRON AND COAL COMPANY
ET AL., PETITIONERS,**

vs.

THE FARMERS' LOAN AND TRUST CO. ET AL.

**Supplemental Brief for Respondents, Moran Brothers
and Henry K. McHarg.**

L. W. CAMPBELL,
Solicitor for Respondents,
Moran Brothers and Henry K. McHarg.



IN THE
Supreme Court of the United States.

OCTOBER TERM, 1898.

LACKAWANNA IRON & COAL Co. <i>et al.</i> , Petitioners,	}	No. 162.
<i>vs.</i>		
FARMERS' LOAN & TRUST Co. <i>et al.</i> , Respondents.		

**Supplemental Brief for Respondents Moran Bros.
and Henry K. McHarg.**

We prepared our brief in this case without waiting for the brief for petitioners. We did this supposing the points made and relied on by them in the Circuit Court of Appeals would be the only ones which they would rely upon in this court. We find, however, that at least one important new point has been made and one important old point has been apparently given up by petitioners. This necessitates the preparation of an additional brief by us. The new point is that petitioners now admit that the rail was not used as part of the current expenses of operation, but was used for "retracking of the entire system," and that because this is so they have "an equitable material-man's lien" on the *corpus* and earnings. The old point, which

is apparently abandoned, is that the rail was used and consumed as part of the current daily expenses of operation, and that their claim was of the same class as coal used for daily consumption; and the case of *Burnham v. Bowen*, a coal case, was the principal case relied on to support the claim. We do not refer to this change in disparagement of petitioners' right to urge it, for as we understand it they have the right to rely here upon any legal proposition that may help out their case, whether it was ever relied on before or not. So that instead of ignoring this new point, we will in the following brief attempt to answer it. Other points made in petitioners' brief will be referred to, but not elaborately, as they are all discussed in our brief already filed.

Petitioners' new proposition is, that "a material-man who furnishes a railroad with supplies which save and preserve the property and enable it to continue a 'going concern,' has an equitable lien upon the income and the corpus of the property superior to that of the mortgage creditors." (Petitioners' Brief, p. 20.)

This proposition is divided into two sub-propositions. The first is, "that property saved and preserved by materials and supplies at the request of the owner is subject to and charged with a lien as against the owner for the value thereof." (Brief, p. 22.) The second is, that "the mortgage creditor by leaving the railway company in the possession of the property authorized it to create any liens thereon which might be necessary to keep up the property and enable it to continue to earn the interest upon the mortgage debt." (Brief, p. 39.)

These sub-propositions are presented separately; arguments made, cases cited, and the conclusion reached by counsel that both are correct. We take issue with counsel and deny their premises, question the soundness of their arguments, and differ from them materially on the conclusions they reach.

Before we enter upon a discussion of the above propositions this court should be reminded that counsel in their brief nowhere claim that the material—the rail—was supplied for or was used by the railway company as a part of its current expenses of operation, but admit that such was not the fact. They say: "The facts in the case at bar make it somewhat different from the usual run of cases decided by this court which involve the doctrine of *Fosdick v. Scholl*, 99 U. S., 235, and the furnishing of the rails to the railway company was not the ordinary case of a periodical renewal of supplies to make good the usual wear and tear upon a railroad or the sale of coal to furnish fuel to its engines" (Brief, p. 20); and they say further: "As the record shows, the track of the railway was worn out," and "there was substantially a retracking of the entire system." (Brief, p. 21.)

We quote from the brief of the petitioners' counsel so that the court may see that all hands are agreed that the rails furnished constituted no part of the current expenses of operation, and that it is conceded that they were used for purposes of reconstruction, or, as counsel say, for "retracking of the entire system."

We also call attention to the fact that counsel nowhere challenge the master's finding of fact that the rail was bought in unusually large quantities, upon the general credit of the railroad company, without any agreement that security should be given or that payment should be made out of any particular fund or in any particular way, and that the claim can not be classed as a current debt. (R., p. 101.) Nor do they gainsay the correctness of substantially the same conclusions of the Circuit Court of Appeals. (R., pp. 134 and 140.) So that the idea that the case contains any of the equities upon which preference has been usually decreed by this court may be dismissed from consideration; but that it is pregnant with facts which have in nearly every case defeated the

claim to priority should be constantly borne in mind. To secure the claimed priority, counsel put forth the above-quoted propositions, and with commendable zeal and ability try to sustain them. An examination of the adjudicated case will show, however, that while the argument is ingenious, this is by no means the first time it has been pressed upon the attention of this and other courts.

By the above propositions and the supporting arguments, the claim to priority is put upon the narrow and uncertain ground that petitioners have an equitable material-man's lien, and that the railway company had the right to create the lien so as to give petitioners priority, on the ground that the railway company was the implied agent of the mortgage creditors because it was left in possession of the mortgaged premises. Both of these propositions must be sustained before priority will be decreed. In other words, if there is no such lien as an equitable material-man or mechanic's lien on a railroad, petitioners fail; or if such a lien can exist, but the railway was not the implied agent of the mortgage creditors in contracting for the material, petitioners fail. But while petitioners apparently must fail if either proposition is unsound, we believe it is likewise true that under the facts of this case and the settled law governing such cases, they must fail if both are sound.

I.

There is no such incumbrance known as a common-law material-man or mechanic's lien on real estate, nor is there such an incumbrance known to or recognized by courts of equity. Nor is there any such lien known to common-law or equity courts as an incumbrance upon or lien against the rents and revenues of real estate in

favor of such material-man or mechanic for the price of improvements erected upon such real estate.

The roadbed of a railroad is generally regarded as real estate, and it is this real estate that petitioners claim their material improved. The rents and revenues of the railway in question consist of money. Petitioners are not now, and have never been, in possession of either the roadbed or the revenues, but have always been out of possession. There is no claim that any promise was made by the railway company to give petitioners a lien on the roadbed or the revenues, or that there was an ineffectual effort to create a mortgage or lien by contract, on either to secure the claim. So the lien must arise out of the transaction by pure operation of law, or by force of some equitable principle, if it exists. We reiterate that such a lien, even between the original parties, is a stranger to both common-law and equity courts.

Phillips on *Mechanics' Liens* (3d ed.), sec. 1, says: "The lien of mechanics and material-men on buildings and the land upon which they are erected, as security for the amount due them for work done and materials furnished, is the 'creation of statute,' and was unknown to either common law or in equity. The idea of lien at common law signified merely the right to hold a thing as collateral security for the payment of debt or performance of duty, and was so inseparably connected with the possession of the subject of the lien that the right arose with possession and terminated with its loss." And same author further says, at section 2, "Although in equity the possession of land is not essential to a lien, and the term is used to denote a charge or incumbrance merely, with no right to the thing itself, yet the courts of equity have so closely followed the general doctrine of the common law as to hold that land belonging to and being in possession of the proprietor and not the builder, the ma-

terials, as far as incorporated in the structure, become annexed to and form a part of the real estate, and vest accordingly as to title and possession. Without special agreement, therefore, no equity arises for a lien upon a mere building contract."

Jones on Liens (2d ed.), vol. 2, sec. 1184, says: "A mechanic's lien upon real estate is wholly a creature of statute. At common law a mechanic has no lien upon a building for labor done upon it." This court, in the case of *Canal Co. v. Gordon*, 6 Wallace, at page 571, in referring to liens of material-men, contractors and mechanics upon land, say: "Liens of this kind were unknown in the common-law and equity jurisprudence, both in England and in this country. They were clearly defined and regulated in the civil law. Where they exist in this country they are the creatures of local legislation."

This court again, in the case of *Van Stone v. Stillwater &c., Bridge Mfg. Co.*, 142 U. S., at page 136, say: "This lien is a creature of the statute and was not recognized at common law."

Text books and decisions could be cited almost without limit, all sustaining our contention that a material-man has no lien, common law or equitable, independent of statute, upon real estate as security for the price of materials furnished to erect buildings or other improvements. Such is the settled law so far as ordinary real estate is concerned, and petitioners' contention to the contrary is unsound. But their contention is that this supposed equitable lien exists on railroads for necessary improvements. This we also deny. This question came up in the case of *St. Louis, A. & T. Ry. Co. v. Matthews*, 75 Texas, 92.

A statute of that State gave a lien to "mechanics, laborers and operatives who have performed labor or worked with teams, tools or otherwise, in the construction,

operation or repair of any railroad," etc. Appellee Matthews furnished to the railway company ties which were placed in the roadbed, and he claimed a lien on the road for the price of the ties. The court held that Matthews' claim did not come within the terms of the statute conferring the lien, and as he had no common-law or equitable lien, he was held to have no lien of any character. The court say:

"The legitimate inference from these averments is that appellee took a contract to furnish ties at a price named, and did so, and that in preparing and delivering them he bestowed his personal services; that he sold ties which may have been prepared and delivered by his own toil, but did not perform manual services in the construction, repair or operation of appellants' railroad.

"Looking to the averments of fact contained in the petition, under a liberal intendment, we are of opinion that the petition does not state facts giving a lien, and that the demurrers should have been sustained."

Jones on Railroad Securities, section 573, says:

"The general lien laws in favor of mechanics and others who perform labor and furnish material for the construction of buildings are usually regarded as having no application to railroads."

And at section 575 he says:

"A railroad bridge is not an improvement within the meaning of that word as used in the general lien law."

Jones on Corporate Bonds and Mortgages (2d edition of Railroad Securities), section 584, says:

"It has sometimes been sought to establish equities in favor of those who have furnished material or money for building or repairing of railroads, on the ground that the property has thus been conserved and rendered capable of profitable use. This is, in fact, an attempt to apply

to railroads the principle adopted by the civil and maritime laws of awarding priority to the last creditor who furnishes necessary repairs and supplies to a vessel. Thus, in *Galveston R. R. v. Cowdray*, a person who had furnished the iron laid upon a portion of the road claimed therefor an equitable lien in preference to an existing mortgage: first, because the mortgage covered the iron only as after-acquired property, and upon the principle of equitable estoppel, which should yield when it comes in conflict with a superior equity; and, secondly, because his property applied to the road had rendered it capable of being operated, when it otherwise could not have been used. The Supreme Court of the United States denied the claim on both points, declaring that the mortgage attached to the property as soon as it was acquired, and that the principle of maritime law contended for had no application.

"Mr. Justice Manning, referring to this case, in giving the decision of the Supreme Court of Alabama, in the recent case of *Meyer v. Johnston*, with reference to the latter principle, said: 'A ship far from home, in distress and without resource, must perish, and perhaps her crew with her, if a bottomry bond given them for repairs and supplies shall not have precedence of other liens upon the vessel. But the court does not consider a railroad on *terra firma* so beyond the reach of help from those who own it, or are concerned in it, as to justify the adoption, in such a case, of the rule relating to a ship abroad, and about to perish.'

"Accordingly, the court, in this case, refused to give precedence to the claim of a contractor for repairing and completing a railroad, although by contract with the company he was to have possession of the property until his claims were paid."

Jones on Corporate Bonds and Mortgages (Second Edition of Railroad Securities), sec. 587, says:

"A claim for materials furnished an insolvent railway company, which is not a lien by virtue of any statute, is not entitled to payment out of the funds aris-

ing from a sale of the property at the instance of prior mortgage bondholders until the bonds are paid. A promise by the receiver to make such payments does not change the case. The ground of the application in this case was that the supplies were furnished to the road while it was run by a lessee, and that when the road came into the hands of the receiver, the parties who had furnished the supplies had an equitable lien upon the funds realized from the earnings of the road. They had no specific lien, legal or equitable, upon the property. The facts of the case were that there were large mortgages upon the road, and the company had become hopelessly insolvent. Application was made to the court to put it into the hands of a receiver in order that it might be operated for the payment of these mortgages. This was done, and the road remained in the hands of the receiver for some years. Subsequently other creditors applied to the court, it being manifest that the mortgages could not be paid in that way, or at any rate that the time would be so long that it was desirable for the interests of all that the administration of the road should be changed; and a sale of the property was ordered and made, so that the parties in interest might realize upon their claims. The court held that the petitioners had no equitable lien upon the proceeds of this sale because the prior mortgage liens must prevail, and these would sweep away the entire fund and would be only paid in part."

"Judge Drummond in making this decision, said, by way of illustration:

"It is precisely like the case of a man who furnishes to the owner of a farm the means of carrying it on, but there is another party who has a lien upon that farm, and it is sold in order that the party who has the prior lien may be paid. Now the fact that the mechanic or laborer has furnished the means of carrying on the farm would not authorize him to come into a court of equity and cut off the prior lien which exists on the farm and prevent it from being paid. These parties ought to be paid. They have a just claim against this road. But it is against an insolvent corporation, and they ask parties

who have a prior right and lien to pay them because those with whom they have dealt can not do so."

The same claim for a superior equitable lien was made by the Lackawanna Company in the case of *Bound v. Ry. Co.* (58 Fed., 473), and while it was found as a fact by the court that the rails furnished were necessary for the operation of the road, and that the president had promised to pay for them out of the earnings, the claimed superior lien was denied. This claim has been asserted in this and other courts in many cases, and has, so far as we are advised, been uniformly denied. So we feel with these lights before us that we can safely say that it is well settled that no such lien exists; and on this point petitioners must fail.

II.

Petitioners second sub-proposition is that the railway company acted as agent for the mortgage bondholders in contracting for the rail and for that reason petitioners are entitled to a priority.

If this is true the mortgagee is principal debtor.

It is claimed that this was an *implied* agency arising from the fact that the railroad company was, as claimed, left in the possession of the railway property. No claim is made that the mortgage creditors had any knowledge of or took any hand in the purchase of the rail or ever agreed that petitioners should have priority. Nor is there any claim that when the rail was purchased and put in the road there had been any default in the interest payments or that the mortgage bondholders were at that time for any other cause entitled to the possession of the railway.

The proposition is, broadly, that any and all railway companies in possession of the railway property which

is incumbered with a mortgage has the implied authority from the mortgage creditors to displace their contract priority with the purchase price—not of current supplies used from day to day to keep the road in operation, but for rail used for “retracking the entire system.”

If this is law, it is very dangerous law, and steps ought to be taken without delay to cause its repeal. Such a law would strike down at a single blow every contract right, every security the mortgage creditor has, and leave him to the mercy of the mortgagor.

There is no such implied agency in the mortgagor arising from possession. A mortgage is a mere security, and the mortgagor is entitled to possession until default. This possession is entirely consistent with the rights of the mortgagee.

The mortgage in this case was recorded and the petitioners had actual notice of its existence.

Jones on Liens, vol. 2 (2d ed.), section 1477, says:

“A mortgagor can not by a contract for the repair of the mortgaged premises subject the property to a lien against the mortgagee without his consent or authority, and it is immaterial whether the mortgagee holds under a formal mortgage or holds the title absolutely as security.”

In the case of *Challoner v. Bouck* (56 Wis., 652) an effort was made to establish this implied agency in the mortgagor in possession of land to incumber it against the rights of a prior mortgagee. That court say:

“If Mr. George Challoner had inquired of Mr. Bouck as to his interest in the property he would doubtless have learned the truth in regard to it. Or if he had inquired of Mr. Bouck whether he was interested in the repairs being made, or whether Mr. Felker was acting as his agent in making them, he would have exercised common prudence and diligence. But he did nothing

of the kind. If we were to hold that he had the right to rely upon the record, and assume from it that Mr. Bouck was the real owner, yet it does not appear that he used any means to ascertain whether Mr. Felker had authority to act for Mr. Bouck in the matter. While, therefore, we might be satisfied that the referee found correctly, upon the evidence, that the repairs on the mill were made by Mr. Felker with Mr. Bouck's knowledge and consent, yet we should be compelled to affirm the other finding, that in the matter of making those repairs Mr. Felker did not act for and was not the agent of Mr. Bouck. The law applicable to that state of facts is laid down in *Lauer v. Bandow* (43 Wis., 556): 'Parol agency to charge a principal's realty ought to be express and clearly established.'

Phillips on Mechanics' Liens (3d ed.), section 225, says:

"The governing principle upon which the adjudications in contests for priority have been based is, that vested rights of purchasers or incumbrancers and, reciprocally, the liens of mechanics, are not affected or displaced, when once attached, by other rights subsequently accruing. The priorities of each are jealously protected from all hostile interference.

"The law imposes on mechanics, like other persons, the necessity to ascertain for themselves the nature of the interest, in the land to be improved, of the persons with whom they contract; and all negligence in this regard is charged to their own account. The contract must be with the owner or his agent, or the plaintiff will fail as against a subsequent mortgagee, and mere evidence of possession by the contracting party is insufficient. To allow the vested rights of third persons, not parties or privies to a contract, to be prejudiced by its terms, would be destructive of the rights of property, and entirely at variance with the office of a lien."

In *Lauer and Another v. Bandon* (43 Wis., 556), an effort was made to establish the implied agency of the

husband to charge the wife's land with a mechanic's lien.

In disposing of the case, the court say :

"In the present case there is no averment in the complaint that the work was performed and the materials furnished by the plaintiffs for the appellant, or that she did any act in respect to the erection of the house which she would not ordinarily have done had the property belonged to her husband. Neither is she charged with any fraud or collusion. The mere fact that she owned the land on which the house was erected is not sufficient to charge her or her estate with the cost of the house. There seems, therefore, to be no foundation for saying that the house was built for her; and the case is not within the principle stated in *Wheeler v. Hall*.

"Our conclusion on this branch of the case is, that the averment in the complaint that the appellant knew of the contract between her husband and the plaintiffs, and consented to and approved it, and that the same was performed by the plaintiffs, with like consent and approval, under her daily view and inspection, is entirely insufficient to raise an implied promise on her part to pay for the house, or to show that her husband really made the contract in her behalf as her agent. (*Bliss v. Patten*, 5 R. I., 376; *Barto's Appeal*, 55 Pa. St., 386; *Fetter v. Wilson*, 12 Ill., 90; *Hughes v. Peters*, 1 Coldw. (Tenn.), 66; *Jones v. Walker*, 63 N. Y., 612; *Kneeland on Mechanics' Liens*, 33.)"

"Although the above cases were decided upon statutes differing somewhat from ours, yet they contain general doctrine which goes to support the views above expressed."

In the case of *Welcome W. Jones et al., Appellants, v. Lucretia F. Walker, Respondent* (63 New York Reports, 612), the court say :

"To charge a wife for work done upon her premises, under contract with her husband, there must be some evidence that he acted as agent and not as principal, and that his contract was for the wife, upon her credit and

with her consent, with knowledge that her credit was pledged, and she is understood to be the contracting party; his agency will not be assumed without any evidence."

Jones on Liens, vol. 2 (2d. ed.), section 1457, says:

"As a general statement of common law, a building erected by the owner of land becomes a part of the realty as soon as it is annexed to the land. It also becomes subject to an existing recorded mortgage of the land. The mortgagee, in a suit to foreclose his mortgage, can not be compelled to sell the building separate from the land, and to allow the proceeds of the building to be applied in satisfaction of a mechanic's lien, before obtaining satisfaction of the mortgage debt.

"Moreover, the materials furnished by a material-man, upon his filing his claim of lien, become subject not only to his own lien, but also subject to the liens of other material-men and mechanics in whose favor liens attach to the premises; for the materials become a part of the entire structure as soon as they are annexed to it.

"A law which attempts to make a mortgage existing prior to the making of any contract for the erection of a building upon the land subject to liens under the statute is unconstitutional."

In *Meyer v. Berlandi* (39 Minn., 438-443; 40 N. W. Rep., 513). Mitchell, J., delivering the opinion, said:

"This is a manifest attempt to displace all prior incumbrances upon, and vested interests in, the property, or at least to postpone them to liens under the statute subsequent in time, so that, for example, a mortgagor and a material-man or laborer, as a result of some arrangement between themselves, without the knowledge or consent of the mortgagee, might improve him out of his prior lien in the premises * * *

"No case ever held that a mortgagor could, without the authority of the mortgagee, expressed or implied, create a lien on the mortgaged property so as to give it precedence of the mortgage."

In the case of *Giles v. Stanton* (86 Texas, 620) an effort was made by a general creditor of a railway company to displace the priority of the mortgage creditors. The right to this priority was in express terms given by a Texas statute, enacted after the execution of the mortgage. In denying the claimed priority, that court says :

"The right to take possession of the road and to appropriate the earnings constituted in part the obligation of the contract, and in so far as the legislature endeavored to give a preference in the earnings to a claim which before its enactment had no lien on such earnings, in preference to the lien of a mortgage made before the law was enacted, giving a lien in express terms, the law violated the obligations of the contract, and was void, as contrary to article 1, section 10, clause 1 of the Constitution of the United States, and of article 1, section 16 of the Constitution of this State.

"Mr. Cooley says: 'If any subsequent law affect to diminish the duty or to impair the right, it necessarily bears on the obligation of the contract in favor of one party to the injury of the other.' (Cool. on Const. Lim., 346)."

In Pindry on Mortgages, vol. 1, section 854, it is said :

"Money expended in improvements by the mortgagor upon the mortgaged premises, or by his grantee subsequent to mortgage, can not be a lien prior to that of the mortgage."

And at section 855, it is said :

"This rule holds the same as to third persons. Thus, if a party makes improvements on the mortgaged land with the consent of the owner, with notice of the mortgage, he has no greater rights than the mortgagor if he had made the improvements, unless a covenant in the mortgage provides for an allowance to the mortgagor in case of foreclosure."

And at section 856 it is said :

"The relation held by the mortgagee does not itself make him responsible for permanent improvements or essential additions made to the estate by the mortgagor, or enable a party furnishing work or material for improvements to maintain a case against the mortgagee without proof of any other facts than is disclosed by the mortgage. There must be a promise on the part of the mortgagee to pay for such work or material or the party can not obtain satisfaction from the mortgagee."

To same effect see *Holmes v. Morse*, 50 Me., 102.

It might be admitted that the implied power exists in a railway company to contract on a credit for necessary current supplies needed from day to day to keep the road in operation, but this is the extent of the power. It certainly has no power to make a superior mortgage on the corpus or an express superior lien against the earnings, so as to bind them after possession is taken by the mortgagee, for retracking the entire system. Such a power can not be conferred upon a railway company by express legislation, except the law be enacted before the mortgage is given. And it is only in cases where the mortgage creditor asks equitable relief that this court considers it has the power to displace the priority in favor of a limited class of claims. Most certainly, no power would be implied to exist in the mortgagor to do an act considered so hostile to the contract priority of the mortgagee which if given expressly by legislation would be held by the courts as void and unconstitutional because it impaired the obligation of contract. Certainly, the court will not presume the existence of such a power. No less than full and cogent evidence of express consent by the mortgagee ought to be tolerated.

From reason and authority it seems clear that petitioners are wrong in the contention that the railway in

contracting for the rail was acting as the agent of the mortgage creditors, and the superstructure builded by ingenious argument upon this unsound foundation must, it seems to us, go the way of all its predecessors. This argument being based largely upon a number of cases cited by petitioners' counsel, we will as rapidly as possible review them.

Review of Petitioners' Authorities.

Shearman v. Assurance Co., L. R. 14, Eq. 4 (Brief p. 23).

This case shows that the real controversy was over the proceeds of the insurance policy and not over the premiums. The plaintiff offered before suit, and stood ready at all times, to refund all premiums paid by Pocknell after his adjudication in bankruptcy.

The opinion in the case was evidently delivered orally, is very short, and only the substance of what the Master of the Rolls said is given. But we find that "He was of opinion, however, that she ought to have accepted the offer made to her before the institution of the suit"—that is, to repay to her all premiums. The plaintiff evidently kept his offer good during the litigation, for we see that it was arranged that the costs be set off against the premiums. The case decides no point involved in this case.

In the Matter of Thorp (Brief p. 23).

The report of this case shows that it is no opinion at all, but a mere statement of issues submitted to counsel for future argument. In the outset it is said :

"The Lord Chancellor (Lord St. Leonards)—I have already stated that I do not mean to decide any question in this matter at present, and that it will be necessary that this matter should be argued with reference to the different questions, very deliberately, before the court."

And, in concluding these issues, the Lord Chancellor said :

"The result, therefore, is, that this is a case in which the parties may, by coming to some reasonable understanding between themselves upon some of these questions, save themselves from very great loss ; but they will determine that for themselves, and consider for themselves what they had best do ; in the meantime, I shall direct this case to stand for the first day after term, and to be regularly argued by the different parties on the points of law to which I have now adverted."

Minnett v. Lord Talbott, L. R. Ir, 1 Ch. D., 143 (Brief, p. 24).

In this case the committee who furnished the funds to make the improvements were members of the club, and they were, by resolutions of the club, authorized to make the improvements. At one of the meetings the following resolution was adopted :

"*Resolved*, That for the purpose of carrying out the contemplated improvements forthwith, the committee be authorized to raise the sum of £500 by debentures bearing interest at £5 per cent.—Agreed to."

On the faith of this resolution the committee made the improvements. The effect of the above resolution, if nothing further was done in reference to issuing debentures, would be to give to the persons making the improvements, with the consent of the club, an equitable mortgage on the premises and property of the club, with the right to maintain an action of specific performance, and compel the issuance of the debentures, or they might have a direct action, as was pursued in that case, and foreclose the equitable mortgage. The case is not in point here.

Munnix v. Purcell, 46 Ohio St. Rep., 102 (Brief, p. 25).

The legal title to the property was in the Archbishop. While there was a bitter and complicated case growing out of the right to hold the property held in trust for the Catholic Church for the private debts of the Archbishop, the case of Hendricks for that portion of his claim which was for improvements, seems not to have been very difficult or complicated, as counsel seems to think.

Hendricks obtained a general judgment in the lower court for the price of the improvements erected by him, and the Supreme Court allowed this judgment to stand. The case, as reported, don't show that Hendricks had or claimed a mechanic's or material-man's lien on the property he had improved. His counsel contended that he should be reimbursed out of the church property generally, and the court properly held that the trust property was chargeable with the trust debts.

The court said, on that branch of the case:

"Such a trustee has power, by contract, to charge the trust property with the reasonable expense of its necessary preservation, improvement and repair, in favor of one who expends money, labor or material for that purpose."

The Archbishop was required to look after the property and keep it in repair. He occupied a trust relation to the property, and for a debt contracted for the benefit of the trust estate he could be sued, and execution would run generally against all the trust property.

The Lackawanna Company was not a trustee of the railway property.

The case decides nothing here.

2 *Story Eq. Jur.* (13th ed.), p. 582, sec. 1237 (Brief, p. 26).

The section quoted and relied on, referred to improvements made upon the premises by a *bona-fide* purchaser of the premises whose title subsequently failed. This statement of the equity rule is a correct one and has general application. But he must be a *bona-fide* purchaser—that is, he must have paid a valuable consideration for the estate, and must have had no notice of the defect or prior incumbrance.

But petitioners admit they had notice of our mortgage, and hence the essential fact to make them *bona-fide* incumbrancers fail.

The author was not dealing with the right of a mortgagor to incumber the estate without the consent of the mortgagee or with priorities. He had already treated of priorities in the first volume.

1st Story's (13th ed.) *Equity Jurisprudence*, p. 567, section 553, says:

"In the course of the administration of assets equity follows the same rules in regard to legal assets which are adopted by the courts of law, and give the same priority to the different classes of creditors which is enjoyed at law, thus maintaining a practical exposition of the maxim, *aequitas sequitur legem*. In the like manner courts of equity recognize and enforce all antecedent liens, claims, and charges, *in rem*, existing upon the property, according to their priorities, whether these charges are of a legal or of an equitable nature, and whether the assets are legal or equitable."

And section 557 says:

"In cases where the assets are partly legal and partly equitable, courts of equity will not interfere to take away the legal preference of any creditors to the legal assets."

Smith v. Smith, Supreme Court Reporter (N. Y.),
p. 164 (Brief, p. 27).

The equitable material-man's lien in this case did not spring out of the mere act of erecting the improvements, as counsel seem to think. "The arrangement was," say the court, "that the plaintiff was to put his own money into a building upon defendant's land, that he might derive a larger revenue from it than he would by leaving it on deposit in a bank, and when built, if he got in any way distressed, he was to have the right to sell the building—it was at his disposal."

The court holds, very correctly and upon the plainest principles, that this was an agreement to give a lien on the property to secure the plaintiff. All the plaintiff's rights grow out of this agreement.

Judge Martin then quotes Pomeroy on Equity Jurisprudence and a number of cases to show, and which do show, that when "the party promises to convey or transfer property as security, creates an equitable lien on the property so indicated, at least as between the parties." The decision rests alone upon the above principle.

We all understand that an agreement to give a mortgage creates an equitable mortgage, and an agreement for a lien creates an equitable lien. And these are the only methods known to courts of equity whereby equitable mortgages and equitable liens are created.

Bright v. Boyd, 1 Story, 478 (Brief, p. 28).

This is an ordinary case of improvements erected upon land by a *bona-fide* purchaser where the title afterwards fails.

As stated above, petitioners are not *bona-fide* purchasers or incumbrancers. The Lackawanna Company had notice of our mortgage when the rail was sold.

The principle announced has no application to this case.

Poland v. The Spartan, 1 Ware's Reports, 130 (Brief, p. 30).

Stevens v. The Sandwich, 1 Peters' Adm. Decs., p. 233 (Brief, p. 30). *The Felice*, B. 40 Fed., 653 (Brief, p. 30).

The above three are admiralty cases, and as counsel concede that admiralty decisions are in no way controlling in courts of equity, we will not pause to comment upon them.

Williams v. Gibes, 20 How., 535 (Brief, p. 35).

That was a contest over the right of certain executors for costs, expenses, and attorney's fees incurred and paid out by them in recovering a fund. At page 537 the court say :

"But it is said that these suits were defended by the executors, while claiming the fund in right of their testator, and hence for the supposed benefit of his estate; that the defense was not made in their character of trustees, and can not, therefore, be regarded as a ground for charging the estate of Williams with the cost of the litigation.

"The answer to this view is, that although in point of fact the defense was made under the supposition that the fund belonged to the estate of Oliver, yet, in judgment of law, it was made by them as trustees, and not as owners, as subsequently judicially ascertained; and as the costs and expenses were properly incurred in the protection of the fund, it is but just and equitable they should be made a charge upon it. The misapprehension as to the right can not change the beneficial character of the expense, when indispensable to its security.

"The duty of a trustee, whether of real or personal estate, to defend the title, at law or in equity, in case a suit is brought against it, is unquestioned, and the ex-

penses are properly chargeable in his accounts against the estate. 2 Story's Eq. Juris., sec. 1275."

In that case, and in all such cases, the party expending the money was a trustee, whose duty it was to conserve and protect the trust estate. When the rail was furnished, and at no time, has the Lackawanna Company occupied any relation of trust or otherwise to the mortgage creditors or railway company. That company was under no obligation, legal or otherwise, to sell the rail to the railway company. There appears to be no analogy between the above case and the case at bar.

Hammond v. Danielson, 126 Mass., 294 (Brief, p. 41).
Tucker v. Warner, 49 N. Y. State Rep., 571 (Brief, p. 41). *Scott v. Delahunt*, 65 N. Y., 128 (Brief, p. 43).
Williams v. Allsup, 10 C. B. N. S., 416 (Brief, p. 44).
In The Canada, 7 Sarvy., 173 (Brief, p. 46). *White v. Smith*, 44 N. J. L., 105, 113 (Brief, p. 46).

The above six cases are cited and relied on by counsel for petitioners as supporting their contention that there was implied agency to create a superior lien for the price of the steel rail.

In all six cases the subject of the lien was personal property, and such personal property was put in the possession of the mechanic or artisan. In the next place, the work done was for ordinary "repairs," and not for rebuilding or reconstructing the hack or boat upon which the work was performed.

In none of the cases was a lien claimed on a railroad or on ordinary real estate.

The distinction in the subject-matter of the lien is important. For before it becomes necessary to inquire whether or not a mortgagor in possession has the implied

power to contract a debt for repairs and to create an equitable mechanic's lien thereon superior to a prior mortgage, when the subject-matter of the lien is real estate or a railroad, it is first to be learned whether at equity or at common law a lien can arise on such property in favor of a material-man or mechanic.

It has been fully shown by the authorities cited by us in the former parts of this brief that material-man's and mechanic's liens on lands are wholly unknown at equity and common law, but are "creatures of statute." And we have also shown that the general lien law has no application to railroads. And counsel in their brief admit, and all the facts in the record show, that the rail was used not for "repairs," but for "retracking the entire system." So the above cases can not control this one, and really have no application to a railroad. But we think it has been shown also from the large number of cases and authorities cited and quoted in this brief that the mortgagor of real estate and railroads have no such implied power as is contended for.

Wood v. Guarantee Co., 128 U. S., 416, 421 (Brief, p. 48).

This was the case of the holders of a part of the coupons of certain mortgage bonds issued by a water works company against the balance of the bonds and coupons, claiming priority on the ground that the coupons were sold in payment of material used in the construction of the waterworks system, and the holder of said coupons sought to shelter himself under the doctrine of *Fosdick v. Scholl*. In passing upon that question this court, in referring to the argument in support of said contention, say :

"The argument is unsound. There are several answers to it. *First*, it overlooks the vital distinction

between a debt for construction and operating expenses. *The doctrine of Fosdick v. Scholl is applicable wholly to the latter class of liabilities.* In the case of *Cowdry v. Galveston Railroad Co.*, 93 U. S., 352, it was settled that the doctrine does not apply where it is a question of original construction. *Secondly*, it overlooks the important fact where there is a diversion of the income of a 'going concern' from the purpose to which that income is equitably primarily devoted, viz., the payment of the operating expenses of the concern. * * * In this case it is not pretended that the money used in paying the 117 coupons in question was income of the waterworks company."

This case decides absolutely nothing for petitioners. Every point decided is against them.

Union Trust Company v. Morrison, 125 U. S., 592 (Brief, page 49).

The case is wholly unlike the case at bar. The Trust Company had a mortgage on a railroad dated **OCTOBER 2, 1871**. The interest was payable semi-annually, and in case of default the trustee had the right to declare the whole debt due and take possession. In **OCTOBER, 1873**, the railway company defaulted, and likewise at every subsequent interest period. One Holbrook had a judgment against the company for \$9,500 and costs, and in **OCTOBER, 1874**—about a year after default by the company in its interest payments—was about to levy an *alias* execution on certain locomotives. The railway company believed the judgment to be void, and in **DECEMBER, 1874**, obtained an injunction against the levy of the execution until the injunction case could be disposed of. Morrison signed, as surety, the injunction bond, and finally had the judgment to pay, amounting to about \$13,000, including interest and costs. To secure him against loss the railway company gave him a chattel mortgage on certain engines of the company.

The mortgage bondholders indulged the company in its repeated defaults, and not until NOVEMBER, 1877—more than four years after the default—did the trustee declare the debt due, file a bill, and cause a receiver to be appointed.

On petition of the receiver, about DECEMBER, 1877, the court authorized him to indemnify Morrison against loss out of funds in his hands. For lack of funds, however, this was not done, and on JUNE 30, 1881, Morrison filed his intervening petition praying to be reimbursed. The Circuit Court granted the relief. Its decree was affirmed by this court,—and properly so, and in accordance with established principles.

By failing to exercise their clear legal right—and we might say duty—to take possession and operate the road after the railway company had become insolvent as shown by their repeated defaults in interest payments, the mortgage creditors impliedly consented that the railway company should operate it for them and in their stead.

After default the mortgage creditors were practically the owners of the road and were under the mortgage entitled to immediate possession. And it is precisely as if the mortgage creditors had taken possession and then appointed the railway company or its officials to conduct, manage, and control the business for them. In equity, under such circumstance, the court will consider that as done which should have been done, and deal with the case as if the mortgage creditors had exercised their right and were in actual possession, and had requested Morrison to sign the bond. In delivering the opinion this court, in referring to the peril of the property by reason of the threatened levy, say:

“The trustees of the mortgage might have prevented

such a catastrophe, it is true, by filing a bill of foreclosure and for an injunction and receiver; but they did not choose to take this course until nearly three years afterwards. On the contrary they allowed the railroad company to continue to use the property and to take care of it for them."

And further on it is said, at page 612:

"The appellants place much reliance on the case of *Burnham v. Bowen*, where it is held that debts for operating expenses are privileged debts to be paid out of current income; and that if such income is divested by the mortgage trustees or the receivers for the improvement of the property such debts will be decreed to be paid out of the mortgage fund. But it was added by way of caution: 'We do not now hold any more than we did in *Fosdick v. Schall*, or *Huidekoper v. Locomotive Works*, that the income of a railroad in the hands of a receiver, for the benefit of mortgage creditors who have a lien upon it under their mortgage, can be taken away from them and used to pay the general creditors of the company. All we then decided and all we now decide is, that if current expenses are used for the benefit of mortgage creditors before current expenses are paid, the mortgage security is chargeable in equity with the restoration of the fund which has been thus improperly applied to their use.' It is this remark on which the appellants rely. It is not our intention, however, to decide anything in the present case in conflict with it. The claim in that case was for operating expenses only, and the rule laid down had special reference to them. The present case is of a different character, based on a *bona-fide* effort made by the intervenor to preserve the fund itself from waste and spoliation after the mortgage was in arrears and the right to reduce it to possession had accrued."

The case is not an authority here, because the rail in the case at bar was sold long before there had been any default in interest payments, and while the company was paying promptly.

In addition to Morrison's equity, he had a chattle mortgage on certain locomotives, and his claim had, by a previous order not appealed from, been ordered paid by the receiver. It was upon all these considerations that he was decreed a priority.

Louisville Railroad Co. v. Wilson, 138 U. S., 501 (Brief, p. 55).

In this case Mr. Wilson, an attorney, intervened in a railway receivership case, and claimed compensation for certain professional services, and asked priority over the mortgage creditors. His claim consisted of three items.

The first was for services rendered under an employment by the railway, made prior to the receivership, to recover certain engines and rent due for their use from another company. The services continued over until after his client, the railroad company, and all its effects were placed in the hands of a receiver. Certain sums of money were recovered by him and by him paid, not to the railroad company, but to the receiver.

The second item was for services rendered certain persons interested in the railway who advanced money to pay employees of the road, and who took, upon his advice, assignment of the pay rolls, and who afterwards secured payment of such claims.

The third item was for services rendered the railway company in an equity suit to enjoin the enforcement of a mortgage on one of the divisions of the road, which appears from the record to have resulted successfully; and by reason of his services he preserved unity of control, and it was claimed that he thereby conferred a benefit on the bondholders by enabling the company to earn interest on the bonded debt.

Only the first item of the claim was allowed by this

court, and that was on the ground that the attorney performed services for the receiver by putting the money he recovered in the hands of the receiver, and that the attorney had an equitable lien on such funds; and he was allowed \$300 for his services in that case.

Milttenberger v. Logansport Railway Co., 106 U. S., 286 (Brief, p. 57).

The opinion contains, en account of the complicated condition of the case, a long history of the proceedings before we come to the opinion proper.

Two classes of claimants asserted priority in that case. One was for claims which arose during the receivership under orders made by the court after all the objecting parties had been made parties to the suit and duly served, and from which orders no appeals were taken. All those claims were created by the court, and they, of course, stand upon a different basis to debts contracted by the company.

Having disposed of those claims, the court, at page 311, comes to the consideration of the claims that arose prior to the receivership. The opinion is silent as to the character of claims that were allowed priority, except by inference. They are referred to in the opinion (top of p. 311) as "due other and connecting lines of roads for material and repairs and for ticket and freight balances."

We judge that this language refers to merely current expenses of operation, for when the principle upon which the allowance of such claims is discussed the court refers to those claims inferentially as "unpaid debts due for operating expenses accrued within ninety days," &c.

So the case decides nothing for petitioners.

Thomas v. Western Car Co., 149 U. S., 39 (Brief, p. 61).

This case decides two very important questions involved in this case.

One is the disallowance of amounts due the car company for rental of cars for six months prior to the receivership, and the other for disallowance of claim for *rebuilding or reconstructing* of certain cars. Both points are in our favor.

In passing on the claim for car rental for the six months prior to the receivership the court, after quoting the Kneeland case say (pp. 111, 112):

"And accordingly all claims for rental of cars prior to the appointment of the receiver were disallowed.

"Tested by the principles asserted in these cases, the claim for car rental that had accrued prior to the receivership can not be maintained, but should have been disallowed.

"The case of a corporation for the sale and manufacture of cars dealing with a railroad company whose road is subject to a mortgage securing outstanding bonds is very different from that of workmen or employees or those who from day to day furnish supplies necessary to the maintenance of the road. Such a company must be regarded as constructing upon *the responsibility of the railroad company* and not in *reliance upon the interposition of a court of equity.*"

And in passing on the claim for repairs and reconstruction of the cars the court allowed the claims for ordinary repairs, but not for rebuilding the cars. (See page 16.)

Kneeland v. Am. Loam Co., 136 U. S., 89 (Brief, p. 61).

In this case the court disallowed a claim for car rental during a prior receivership of the road.

It is in this case where Mr. Justice Brewer used the often-quoted language about no one being compelled to deal with a railroad, etc., quoted in our principal brief, pages 32 and 33.

The case decides nothing to sustain the claim here asserted.

Kneeland v. Luce, 141 U. S., 491 (Brief, p. 63).

The question in this case was as to whether receivers' certificates issued by order of the court, with the express consent of the prior mortgagee, were entitled to priority in their payment as against such consenting mortgage. The headnotes state this case fully.

This court held, upon the plainest principles, that the receivers' certificates were, on account of such consent, entitled to priority.

Olcott v. The Supervisors, 16 Wallace, 678 (Brief, p. 64).

The case decides nothing here, as is shown by the statement of Mr. Justice Strong at the beginning of the opinion, on page 688. He says :

"Whether the act of Assembly of the State of Wisconsin, approved April 10, 1887, under which the county orders or promissory notes sued upon in this case were issued was a lawful exercise of constitutional power is the only question in the case."

Burton v. Barbour, 104 U. S., 126 (Brief, p. 63).

The only question involved, and the only one decided, was that a receiver could not be sued in a court other than the appointing court without leave of that court.

Wallace v. Loomis, 97 U. S., 146 (Brief, p. 65).

This case simply reaffirms the settled doctrine that a court of equity having property under its control may legally authorize the issue of receivers' certificates.

While the rule announced in the cases cited by petitioners' counsel may apply to chattels under circumstances surrounding those particular cases for ordinary

"repairs," the rule does not apply to real estate and railroads for permanent improvements and betterments.

Jones on Corporate Bonds and Mortgages (2d edition of Railroad Securities), section 606, says:

"The doctrine of *Fosdick v. Schall* has thus far never been applied to any case other than that of a railroad. The case itself laid great stress on the consideration that a railroad is a peculiar property, of a public nature, and discharging a great public work; and it has been repeatedly decided that this equitable doctrine is not applicable to other corporations."

And it might well be added that the rule in other cases has no application to this doctrine, for such is the effect of the cases. At any rate, counsel has cited no case where this extraordinary power has been held to exist in a railroad company.

III.

Petitioners' second point is that the mortgage gave no lien upon the earnings of the road after it was placed in the hands of receivers in causes 185 and 198, and that as one interest payment was made these bondholders by the receivers in cause 198, that to the amount of such payment there was a division, &c.

We have already presented our views of this question in our principal brief, pages 14 to 25, and a repetition would be useless.

We there attempt to answer this on the ground, among others, that the facts in the record show that petitioners' claim was not a current debt for operating expenses, but was a general debt of the railway company for rail sold it for purposes of general construction, and the conclusion was reached by us that petitioners could not complain of division, if there had been any in fact, for

it is only the favored few—the current expenses creditors—who can justly complain of division—a general creditor, never!

We pause to say that petitioners having agreed with us on the facts—that is, that their claim is not of the current debt class—it only remains for this court to say whether petitioners can complain of division.

We deny the claim that there was a division, and ask the court to read our brief on that point.

IV.

Petitioners' counsel contend under their fourth, fifth, and sixth points that the mortgage did not cover the income after possession was taken, and that there should be a *pro-rata* distribution of the income.

The point is fully discussed by us in our brief, pages 14 to 25, and what we say there will not be repeated here.

This question is discussed by counsel as if it depended solely upon the terms of the mortgage. Indeed, the mortgage so plainly gives a lien on the income after possession is taken, we feel that the whole question could with safety be allowed to rest on the terms of the mortgage alone. But that is not at all necessary, for the mortgage bondholders have a lien superior to petitioners' claim on the revenue arising from the operation of the road by the receivers, on two distinct grounds:

First. The mortgage in plain terms gives it.

Second. This superior lien was acquired by filing the bill to foreclose and by causing the property to be placed in the hands of a receiver on the application of the trustee in the mortgage. In other words, by an equitable levy on the income.

These questions in reference to this particular mort-

gage and equitable levy, on this particular income, were raised, fully argued, and, as we supposed, finally settled and put at rest in the case of *Geo. E. Downs v. Farmers' Loan & Trust Co.* (79 Fed. Rep., p. 221).

The terms of the mortgage relied on by us as conferring a lien upon the income will be found on Record, page 15, and is as follows:

"And in case the said Houston and Texas Central Railway Company shall fail to pay the principal, or any part thereof, or any installment of the interest, or any part thereof, on any of said bonds at any time when the same shall become due and payable according to the tenor thereof and for sixty days after having been demanded, it shall be competent for the said trustee, its successors or assigns, to enter upon the said railway and premises and property herein conveyed, by its attorneys and agents, and take possession of same without let or hindrance of the said first party and every part and parcel thereof, and the appurtenances, and appoint an agent to operate and manage the same, and receive the revenue and income thereof, applying the said funds, after deducting taxes, necessary expenses and counsel fees, to keep the same in good order and repair, and the surplus to pay the principal and interest of all the bonds which may be due and outstanding, and secured hereby, pro rata, and thereafter, to the payment of any contributions due to the sinking fund herein established. And upon the request of the holders of one-fifth in amount of the bonds so in default which may be at any time outstanding under this deed of trust, it shall be the duty of said second party, by its president or agent duly appointed in its behalf, to enter upon and take actual possession, with or without entry, or foreclosure of said railway and property herein described, and all and singular each and every part and parcel thereof, and assume its management until the arrears of both principal and interest be paid, or the property sold, as herein described, receiving the rents, revenue and income thereof and applying them in the same manner as above stated."

The Court of Appeals, after hearing the same arguments and reading the same cases cited, decided that the mortgage bondholders had a lien on the income after possession was taken.

We will not undertake to quote from the opinion ; but as our arguments in answer to all arguments made denying our lien on the income, we cite this court to that opinion.

The lien is equally well secured to us by the equitable levy on the income.

This point was raised and settled in the case of *Sage v. Memphis, &c., Ry. Co.*, 125 U. S., 361. That was a case where Sage, a judgment creditor, having no mortgage, filed a bill and caused a receiver, to be appointed, of the railway property. Net income was accumulated by the receiver. This net income was claimed by the mortgage bondholders, who had a mortgage giving a lien after they had taken possession. But they never took possession or made any move to have a receiver appointed.

This court, speaking through Mr. Justice Harlan, in delivering the opinion in that case, at page 379, said :

“ But we do not perceive any legal ground upon which they are entitled to the net earnings of the property, while it was in the hands of the receiver, in a suit instituted by a judgment creditor for the protection of his own interests and not of the interests of the trustees or of the bondholders or of other creditors. This suit was, in effect, an equitable levy.”

Sage put the property in the hands of a receiver to protect his interest, and the complainant in this case pursued the same course. The mortgage of the bondholders in the Sage case contained a clause like ours, and this court conceded in its opinion that their rights would

have been superior to those of Sage's if they had taken steps to put the property in the hands of a receiver.

So it seems from the foregoing that it is clear that we have a lien on the income.

This disposes of all the points raised in petitioners' brief, except the general discussion of their claimed or supposed superior equities which may be found running throughout the brief.

In concluding this brief, we desire to notice the points made on that branch of the case.

The Equities of the Case.

Petitioners have stated the equities of their case and the principles upon which they rely, and have recited the facts which they claim are in the case to support the claimed equities, and have left it to us to state such equities as we have, if any.

Our purpose in presenting the equities of the case is to examine the grounds of petitioners' claim and to compare the equities of the petitioners and respondents in the light of the record. And while we do this as an advocate, we shall not intentionally omit a single fact or circumstance in the record which will be of benefit to petitioners, or attempt to color the facts in favor of respondents.

The alleged facts upon which petitioners seem to rely to sustain their claimed superior equities, are :

First. That they sold the rail to the railway company on a credit and they have not been paid for, and that the debt is just and should be paid.

Second. That when the rail was sold to the railway company its track was practically worn out and in the condition of dilapidation as reported by the master.

Third. That the rail saved and preserved the property and kept it a "going concern" and enabled the railway company to continue its existence.

Fourth. That on account of the sale of this new rail, old rail was taken up and sold for a large sum of money, which came into the hands of the receiver.

Fifth. That the Lackawanna, with full knowledge of the situation, and appreciating the importance to the railway company of the supplies furnished, sold the rails, took no collateral security, and expected to be paid out of the income.

Sixth. That the Lackawanna Company in selling the rail relied upon the fact that its supplies saved and preserved the property, kept it a going concern, and conferred a benefit upon the mortgage creditors.

Seventh. That with the rail sold the track of the railway company was practically rebuilt.

This is not the language in which the claimed facts are stated, but their substance will, we think, be found in the above seven subdivisions, and petitioners apparently rely on no other facts.

It will be noticed that in the statement of the alleged facts it is admitted that respondents had, when these rail were sold, a valid subsisting prior mortgage on this property, and that the Lackawanna Company had notice of its existence.

It is not claimed that the mortgage creditors were consulted in the matter of buying these rail, or as to the advisability of making the purchase of the rail on credit.

It is not claimed that they even had any knowledge of the purchase.

It is not claimed that the mortgaged premises, consisting of 54 miles of railway and about 250,000 acres of land, was not ample security for the mortgage debt, which at that time was but little over \$1,000,000.

It is not claimed that a single default had ever been made on an interest payment due on these bonds prior to the purchase of the rail.

It is not claimed that a single additional dollar of net revenue was earned over and above what was being earned before the purchase.

It is not claimed that the property sold for a single dollar additional on account of these rails.

It is not claimed that after said rails were bought and put on the road that the interest on the mortgage debt was regularly paid, or that the mortgage indebtedness was better secured thereby, and that no trouble was ever afterwards experienced by them in the collection of their principal and interest.

No! Counsel would not say so. They couldn't, for tested by the record, every fact which petitioners' counsel failed to state, as indicated above, is substantially an affirmative fact, and all the alleged facts relied on to support the superior equity are wholly without existence except numbers 1, 2, and 7.

In other words, petitioners' case as made by the record is an ordinary case of a sale of rails by one corporation to another on a credit, and which have not been paid for, and that the sale was made and understood to be for the purpose of retracking the road of the railway company without the shadow of any benefit to the mortgage creditor, but which in our judgment was the immediate cause of all the subsequent troubles and disasters to railway and bond creditors, and the precipitation of this litigation, which has lasted more than fourteen years, causing a loss to the bondholders of hundreds of thou-

sands of dollars, to say nothing of court costs, attorneys' fees, and other expenses of litigation.

But we desire to examine more minutely petitioners' alleged equities as against the mortgage creditors.

The chief ground of equity is that the rail saved and preserved the property and kept it a "going concern," and in that way aided the security—conferred a benefit on us. There is not the shadow of a fact in the record to justify this claim. None of the evidence is in the record, and the only facts are those reported by the master; and he does not, in the remotest, hint at the question as to what effect the rail had on the security, or whether or not the security was ample with the old rail, or whether the laying of the rail kept the road a "going concern" as claimed.

Petitioners allege in their petition that all these and many more beneficial results followed the laying of the rail; but the master, to whom was committed the authority to hear the evidence and report the facts, does not so find.

If the mortgage security was insufficient just before the rail was furnished, but afterwards became better or first class as a result of the laying of the new rail, that fact was doubtless susceptible of proof.

If the road was not in fact a "going concern" and promptly meeting its obligations, including bonded interest, that fact could have been proven.

If the laying of the rail increased the net earnings of the road or caused it to sell for a better price, that fact could have been proven.

If, in short, any fact existed which showed that a dollar has come, or will ever come, into the pockets of these mortgage creditors as a result of the laying of these rail, it looks like that fact could have been proved, and the master could have been induced to so report.

We find no such fact in his report. But while we find a total absence of any fact showing or tending to show the effect of the rail on the mortgage security, we do find many facts in the master's report which show that very soon afterwards a dire calamity followed, and from the effect of which these bondholders have not recovered, and will never recover. This calamity was the throwing of the whole system in the hands of receivers, in about a year and a half after the last delivery of rail, by a general creditor, and which engendered a bitter and extended litigation, which lasted for more than thirteen years, resulting in a loss to the mortgage creditors of more than \$200,000 of their debt, to say nothing of expenses of litigation.

Whether there is *causal* connection between the incurring of this large debt for rails, and its rapid payment out of the earnings of the road in preference to other debts of the company, and the precipitation of the receivership and the resultant losses may not be clear.

One thing is clear: That for more than twelve years preceding this large purchase of rail the bonded interest was promptly paid, and for more than twelve years immediately after not a dollar of principal or interest was paid on bonded interest except the interest for one year paid by the receivers in cause 198.

Another thing is clear: This railway company was the pioneer road of Texas, built in ante-bellum times, and had weathered every storm, not excepting the "late unpleasantness," and was promptly meeting its obligations until the purchase of this rail, but in less than a year and a half it was in the hands of receivers, and in less than three years all its property was sold under foreclosure decrees and its "continued existence" collapsed and its name passed into ancient history.

The cause and effect may not connect, but whatever

may have caused these financial disasters, it is clear that these bondholders derived no benefit from the laying of these rail, and if they were sold by the Lackawanna Company as a friendly act to us and the road to keep it a "going concern," and to "continue its existence" and "enable it to pay its interest," we are disposed to exclaim, The Good Lord "deliver us from our friends!" Petitioners have shown no equity against us—that is, no benefit conferred upon us, and our mortgage being valid and being first in time is first in right.

The remarks of this court in the case of *Railway Company v. Wilson*, 138 U. S., 501, in passing on the claim of an attorney who has successfully enjoined certain mortgage creditors from selling one division of the road. He claimed that his services resulted in unity of control and enabled the road to earn bonded interest. But the facts in that case, like this, showed no bonded interest accumulated and paid to the bondholders.

This court say, on page 509 :

"It can not be that security bondholders are liable, either in law or in equity, for the expenses incurred by their debtor in carrying into effect a scheme which the latter believes will enable it to pay its interest to them but which in fact does not accomplish such result. It was the debtor's act, and if it failed of accomplishing hoped-for results the party employed must look to his employer alone for compensation and can not charge the bondholders therefor, on the theory that it was believed that it might inure to their ultimate benefit."

The facts collated and the authorities cited in this brief show, we think, that petitioners' claim for an equitable material-man's lien does not exist; that the demand for *pro-rata* distribution of the income must be denied, and the claimed superior equities arising from alleged benefits conferred have disappeared.

This leaves the case where it belongs.

A sale of rail on the general credit of the company, for purposes of construction, and that the debt can not be classed as a current debt, and the claimed priority ought to be denied.

We present our views on this subject fully in our brief already filed. We refer to pages 1 to 13 for a full discussion of this subject.

Respectfully submitted.

L. W. CAMPBELL,
*Solicitor for Respondents, Moran
Bros. and Henry K. McHarg.*



Statement of the Case.

LACKAWANNA IRON AND COAL COMPANY *v.*
FARMERS' LOAN AND TRUST COMPANY.CERTIORARI TO THE CIRCUIT COURT OF APPEALS FOR THE FIFTH
CIRCUIT.

No. 22. Argued March 10, 1899. — Decided January 29, 1900.

The principles announced in *Southern Railway Co. v. Carnegie Steel Co.*, *ante*, 257, reaffirmed; but the claims filed in this suit were held not to be current debts chargeable upon the current receipts of an insolvent railroad company in the hands of a receiver in preference to the claims of mortgage creditors.

THE Houston and Texas Central Railway Company, a corporation of Texas, formerly owned and operated in that State several lines of railroad, as follows: From Houston to Denison, a distance of 345 miles, known as the main line; from Hempstead, on the main line, to Austin, a distance of 118 $\frac{3}{4}$ miles, known as the Western Division; and from Bremond, on the main line, to Ross, a distance of 58 miles, known as the Waco and Northwestern Division. It also owned lands donated by the State in aid of the construction of its roads.

Prior to April 1, 1881, the Company had executed various mortgages or deeds of trust, namely: 1. A mortgage dated July 1, 1866, covering the main line and ten sections of land for each mile, known as the main-line first mortgage, in which Easton and Rintoul were substituted trustees. 2. A mortgage dated December 21, 1870, covering the Western Division and ten sections of land for each mile thereof, commonly known as the Western Division first mortgage, in which the same persons were substituted trustees. 3. A mortgage dated June 16, 1873, covering the Waco and Northwestern Division (to be hereafter referred to as the Waco Division) and also 6000 acres of land for each mile thereof, commonly known as the Waco and Northwestern Division first mortgage, in which the Farmers' Loan and Trust Company, a New York corporation, was trustee. 4. A mortgage dated October 1, 1872,

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covering the main line and Western Division as a second mortgage and 3840 acres of land per mile of completed road, commonly known as the main line and Western Division consolidated mortgage. 5. A mortgage dated May 1, 1875, commonly known as the Waco and Northwestern Division consolidated mortgage, and covering the Waco Division and 6000 acres of land per mile of completed road. 6. A mortgage dated May 7, 1877, commonly known as the income and indemnity mortgage, and covering all the property of the Railway Company. 7. A mortgage dated April 1, 1881, commonly known as the general mortgage, and covering all the property of the Company.

The present suit, designated in the Circuit Court by the number 227, was brought April 6, 1889, by the Farmers' Loan and Trust Company to obtain a decree of sale of the property covered by the mortgage of June 16, 1873, on the Waco Division. On the same day Charles Dillingham, who was already receiver and in possession of the railway property of the Houston and Texas Central Company, was appointed receiver of all the railway property and property covered by the first mortgage of the Waco Division with power to operate the same, and was directed to keep separate accounts of the expenditures and earnings of that Division.

During the progress of the cause the Lackawanna Iron and Coal Company, a Pennsylvania corporation, intervened by petition, asserting an equitable lien, prior to the claims of bondholders, on the mortgaged property for the value of steel rails alleged to have been furnished by it and laid on the Waco Division. Subsequently the Pacific Improvement Company, a California corporation, became the assignee of the claim of the Lackawanna Company, and was made a complainant with the latter company.

From a report made January 13, 1896, by a special master appointed to find and report upon the subject-matter of the intervening petition, the following facts appear:

Pursuant to a written contract with the Houston and Texas Central Railway Company, dated December 28, 1882, the Lackawanna Company in the year 1883 delivered to the

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former 5020 tons of steel rails at the price of \$40.40 per ton, in payment for which the Lackawanna Company received ten promissory notes of the Railway Company, payable at six months from their respective dates, amounting with interest to \$206,932.16. These notes were all paid either at their maturity or at the maturity of other notes given in renewal thereof.

Pursuant to another contract dated April 26, 1883, between the Lackawanna Company and the Railway Company, the former delivered to the latter in the year 1883, 5009 tons of steel rails at \$39.50 per ton, and received in payment therefor the Railway Company's ten promissory notes dated respectively June 21, 22 and 23, 1883, August 10, 14 and 15, 1883, and September 6, 11, 15 and 20, 1883, each payable six months after date, and aggregating, with interest, \$201,346.64 — the Railway Company being entitled, under the contract, to renew the notes at maturity for a further term of six months by paying the interest at six per cent or adding the interest to the new notes. As these notes matured, the payment of so much of the debt as was not satisfied at maturity was extended until, in process of settlements and extensions, the Railway Company, in the satisfaction of the balance due the Lackawanna Company under the contract, executed its eight promissory notes payable four months from their respective dates, with six per cent interest from maturity. These notes aggregated \$118,000. In the negotiations resulting in this settlement the Lackawanna Company demanded that the Railway Company should secure the renewal notes by the hypothecation of collaterals. In compliance with that demand the Railway Company deposited with the Lackawanna Company, when the renewal notes were delivered, 170 first mortgage bonds of the Galveston, Harrisburg and San Antonio Railway Company of the face value of \$170,000. At the date of the master's report, January 13, 1896, the value of those bonds was \$157,250, or 92½ per cent of their face value. They were in the possession of the Pacific Improvement Company, as assignee of the Iron Company. No interest on the bonds had been collected by the Iron Company or by the Railway Company, but the

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interest had been collected by the Southern Development Company. It was agreed before the special master by the parties in interest that the court should consider the 170 bonds as sold for \$157,250 on December 23, 1895, and should credit that sum, as of that date, upon the claim of the Iron Company or of the Southern Development Company.

On the 30th day of October, 1883, — nearly *six years before the present foreclosure suit was brought*, — the Lackawanna Company and the Railway Company made another contract in addition to those above mentioned, under which the former delivered to the latter, during the months of February, March, April and May, 1884, 8552 tons of steel rails. That contract was similar in its general terms to those of December, 1882, and April, 1883. It provided for the delivery by the Lackawanna Company of 10,000 tons of Bessemer steel rails at \$36.60 per ton, as nearly as practicable between February 1 and August 1, 1884, at the rate of 1500 to 2000 tons per month. It also provided that upon the delivery of each 500 tons of rails payment should be made therefor either in cash or in the notes of the Railway Company payable at six months from the average date of delivery, with six per cent interest from such date, the purchaser to have the privilege of renewing the notes before their maturity for a further term of six months by paying the interest or adding the same to the renewal notes. In March and April, 1884, the auditor of the Railway Company made a statement or voucher of rails then delivered under the contract. That statement passed into the hands of the treasurer of the Railway Company with a memorandum that notes were to be issued therefor payable at twelve months from their respective dates. In conformity with that memorandum the Railway Company executed and sent to the Lackawanna Company eight notes, payable twelve (instead of six) months from their respective dates. The latter Company thereupon notified the Railway Company of the error, but the notes as executed were received as a matter of accommodation to the Railway Company.

Afterwards, in April and May, 1884, the Railway Company, in settlement of the balance due for the 8552 tons of rails,

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executed and delivered to the Lackawanna Company nine promissory notes payable at six months from their respective dates, with the option in the maker of renewal for a like term. Each of those notes were renewed for six months for like amount as the originals, and their aggregate amount was \$327,175.50. This sum, added to the \$118,000 above referred to, made \$445,175.30, the aggregate principal amount due to the Lackawanna Company, not including the \$157,250, the amount at which the 170 bonds delivered as collaterals were valued.

All the rails delivered under the first contract, and about one half of those delivered under the second contract, were paid for by the Railway Company prior to the appointment of any receiver of the property; but the remaining half under the second contract, and the rails furnished under the third contract, had not been paid for when the master's report was filed.

The second contract for rails was made one year and ten months prior to the appointment of the receiver in cause numbered 185 (to be hereafter referred to), about three years and three months prior to the appointment of the receiver in consolidated cause numbered 198 (to be presently referred to), and about six years prior to the appointment of the receiver in this cause. The third contract was made about sixteen months prior to the receivership in cause 185, about two years and nine months prior to the receivership in consolidated cause 198, and about five years and six months prior to the appointment of the receiver in this cause.

About 6.2 miles of the railway of the Waco Division (the part of the railway covered by the mortgage to the Farmers' Loan and Trust Company) was laid with the rails furnished under the first two of the above contracts, but it was not shown what proportion of those rails were furnished under each of the contracts; 30.8 miles of the railway were laid with rails furnished under the third contract. The old iron rails removed from the 37 miles of the Waco Division, upon which the above rails were laid — 2960 tons — were received by the receivers in cause No. 185, and were sold by them in 1885 at the price of \$13 net.

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The master's report contained the following :

"I find that the debt for which the Lackawanna Company claims payment in its petition herein cannot be classed as a current debt made in the ordinary course of business, as those terms seem generally to be understood, yet it appears that at the time when the contracts hereinbefore mentioned were entered into between said Lackawanna Company and the defendant Railway Company that the condition of the track of the defendant Railway Company was such that the demand for new rails upon the most worn portion of the roadway was practically imperative. For a number of years prior to December, 1882, only about 5000 tons of new rails had been purchased. The road north from Houston for 90 miles was built in 1857-1861, and thence northward to Denison, 1867-1872. The Western Division leading to Austin was constructed in part prior to 1861, and completed in 1873, and the Waco Division was completed about 1875. The condition of these roads was bad, except such portions as had been relaid with 5000 tons of rails purchased prior to December 28, 1882. There was continual breakage of rails and wrecking of trains, the track was unsafe, and was generally so regarded, not only by 'railroad men,' but by the travelling public; the damage to merchandise, rolling stock, etc., was continuous, and the need for new rails appears to have been 'absolutely necessary as a preservation of human life, the loss of which was liable to occur at any moment.'

"I find that when the aforesaid contracts were made with the said Lackawanna Company both seller and buyer expected the debts to be paid from the net income of the railway; that the credit extended under said contracts was at the request of and for the accommodation of the defendant Railway Company and upon its general credit. That said sales were made without any stipulation that security should be given by the defendant company for said rails, or that payment therefor should be made out of any particular fund or in any particular way; that said sales were for an unusually large amount of rails, and the defendant was unable to pay cash therefor, and there was no other way of obtaining said rails except upon

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credit ; and petitioner herein at the time of said contracts and sales had knowledge of the mortgage of June 16, 1873, given by the defendant Railway Company upon the properties of its Waco and Northwestern Division to secure the first mortgage bonds, which said mortgage has been herein foreclosed. I find that the steel rails supplied by said Lackawanna Company under the aforementioned contracts, 18,581 tons, were placed in the track of the defendant Railway Company as soon as received."

The bonded debt of the Railway Company on January 1, 1885, was \$16,874,500. The interest on all classes of its bonds payable in 1894, amounting to \$1,194,200, was paid as it matured. The Railway Company first made default in the payment of interest on its bonds January 1, 1895, on which day the interest on first mortgage bonds became payable.

The Southern Development Company, a California corporation, on the 16th day of February, 1885, instituted suit against the Houston and Texas Central Railway Company, asserting a claim against it for about \$600,000 for money loaned at various times. This was cause No. 185. It set forth in its bill the embarrassed condition of the Railway Company, the danger of its property being scattered, wasted and lost, and asked that the Company's property be put in the hands of receivers, and a decree passed directing that out of the rents, revenues, issues and profits coming into the hands of the receivers, after payment of costs of administration, operating and other necessary expenses, the claims of the plaintiff, the Southern Development Company, with interest and costs be paid. On the motion of that Company, Clarke and Dillingham were appointed receivers of the property. They immediately qualified as receivers and took possession of the property. An amended and supplemental bill was filed making Easton, Rintoul and the Farmers' Loan and Trust Company defendants as trustees of the various mortgages upon the Railway Company's property. Clarke and Dillingham continued to act as receivers until about July 10, 1886, when they delivered possession of the property and the revenues in their hands to Easton, Rintoul and Dillingham who had previously

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been appointed joint receivers of the Railway Company under bills filed by the trustees of certain mortgages on the main line and Western Division, and also by the Farmers' Loan and Trust Company as trustee in the general mortgage of the Houston and Texas Central Railway Company. The last-named litigation was known as cause No. 198.

In cause No. 185 the Lackawanna Company intervened by petition, and asked to be made a coplaintiff. It prayed that an account be taken of its several demands, that the amount thereof with interest be paid out of the net revenues of the Railway Company, and be declared a lien thereon and upon all the property of the Company superior in rank to the claims of the trustees and to the mortgage bonds and coupons issued under their various deeds of trust.

To the bill of the Southern Development Company, Easton and Rintoul, trustees, demurred generally and specially. The demurrer was sustained, and the bill and supplemental bill were dismissed with costs on the 27th day of May, 1886, but without prejudice to the rights of the complainants to assert their claims, if any they had, in such manner as they were advised. By the same decree Clarke and Dillingham were discharged and ordered to turn over all the property and effects of the Railway Company together with its accrued revenues in their possession to Easton, Rintoul and Dillingham, who had then been appointed joint receivers of the Railway Company under an order made in the "Consolidated Cause No. 198," *Easton and Rintoul, Trustees, and the Farmers' Loan and Trust Co. v. Houston and Texas Central Co. et al.* — the constituent suits of such consolidated cause being causes Nos. 198, 199 and 201, which were bills of foreclosure against various parts of the railway.

The three mortgages declared on in causes 198, 199 and 201 were duly foreclosed by final decree entered in the consolidated cause on the 4th day of May, 1888, and on September 8, 1888, all the property of the Railway Company was sold under that decree, George E. Downs becoming the purchaser of the Waco and Northwestern Division, subject, however, to the particular mortgage sought in this suit to be foreclosed,

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namely, the mortgage of June 16, 1873, known as the Waco Division first mortgage, the Farmers' Loan and Trust Company being the trustee therein. The sale was also made subject to the right which the court reserved by the decree (to use the words of the master in his report) to charge upon the property or any part thereof the payment of any amount that might be found to be due and payable by reason of intervening petitions theretofore filed in that cause and be entitled to priority over the mortgage debts referred to in the decree.

From February 20, 1885, to the date of the report, the property of the Railway Company, forming the subject-matter of the receivership in this cause, was continuously in the possession of the court under proceedings in suit No. 185, and thereafter in suits Nos. 198 and 227.

The master found and reported that no interest had been paid on the bonded indebtedness by either of the receivers in this cause; that Alfred Abeel, receiver in this cause, had expended under the orders of the court \$46,505.40 for betterments and permanent improvements from December 10, 1892, to September 3, 1895, consisting of bridges, shops, roundhouse, car shed, water stations, locomotives, chair car and fencing; that no part of the income arising from the operation of the road and no part of the proceeds of sales of old rails, old iron, old cars and engines, coming into the possession of the receivers in causes 185 and 198, ever came into the possession of the receivers in this cause, and it did not appear that any part of the equipments purchased by the receivers in causes 185 and 198 ever came into the possession of the receivers in this cause; that the evidence failed to show that any improvements and betterments of the property, added to the property of the Houston and Texas Central Railway Company by the receivers in causes 185 and 198, were made *on the Waco Division*; that prior to April 6, 1889, no separate accounts were kept of the receipts and disbursements of the Waco Division, but the same was operated as a branch of the general system of the Houston and Texas Central Railway Company, and the evidence failed to show what, if any, of the expenditures made by the receivers in causes 185 and 198 for extraor-

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dinary repairs, betterments and improvements, and for operating and running expenses, were made for the Waco Division and what portions for other divisions of the Houston and Texas Central Railway Company, and this was true also as to receipts and income; that the receivers in cause 185 had on hand in cash at the opening of business on January 21, 1886, \$175,393.65, but it did not appear that any part of that fund came to the hands of the receivers in this cause; and that the receiver in cause 198 had on hand at the beginning of business on April 6, 1889, cash amounting to \$215,842.45, but it did not appear that any part of that sum came to the hands of the receivers in this cause.

The mortgage given by the Railway Company to the Farmers' Loan and Trust Company, dated June 16, 1873, and herein declared on, contained the following provisions:

"And in case the said Houston and Texas Central Railway Company shall fail to pay the principal, or any part thereof, or any instalment of the interest, or any part thereof, on any of the said bonds at any time when the same shall become due and payable according to the tenor thereof, and for sixty days after having been demanded, it shall be competent for the said trustee, its successors or assigns, to enter upon the said railway and the premises and property herein conveyed, by its attorneys and agents, and take possession of the same without let or hindrance of the said first party, and every part and parcel thereof, and the appurtenances, and appoint an agent to operate and manage the same, and receive the revenue and income thereof, applying the said funds, after deducting taxes, necessary expenses and counsel fees, to keep the same in good order and repair, and the surplus to pay the principal and interest of all the bonds which may be due and outstanding, and secured hereby *pro rata*, and thereafter, to the payment of any contributions due to the sinking fund herein established. And upon the request of the holders of one fifth in amount of the bonds so in default which may be at any time outstanding under this deed of trust, it shall be the duty of said second party, by its president or agent duly appointed in its behalf, to enter upon and take actual possession with or without entry

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or foreclosure of said railway and property herein described, and all and singular each and every part and parcel thereof, and assume its management until the arrears of both principal and interest be paid, or the property sold, as herein prescribed, receiving the rents, revenues and income thereof, and applying them in the same manner as above stated. It is, however, expressly agreed that the said party of the first part may dispose of the current net revenues and income of all the said property and railway hereby conveyed in such manner as it shall deem best, until default shall be made in the payment of the interest or principal of said bonds, or of any one or more of them, and shall have the right to sell and dispose of any of such real estate or other property as it may own or acquire, which may not be needed or required for the purposes and business of the said Waco and Northwestern Division, except in the case of the six thousand acres per mile of completed road, and which sale and conveyance of such outside property shall transfer the said property and title free from incumbrance of this mortgage or deed of trust, and to change its tracks and make any and all alterations necessary for the benefit of the same."

That mortgage contained no provision authorizing the trustee, if it acquired possession of the railway under that instrument, to pay any floating debt or debts of the mortgagor company out of the gross earnings of the railway.

During the receivership of Clarke and Dillingham, in cause 185, they received revenues from the operation of the railway, from February 23, 1885, to January 21, 1886, \$2,758,487.40, and paid out for operating expenses, taxes, etc., for the same period, \$2,137,322.44, leaving a surplus of \$621,164.96. From January 21 to July 10, 1886, they received \$1,143,731.05, and paid out for operating expenses during the same period \$1,341,753.85, leaving a deficit for that period of \$198,022.80, but leaving a net balance from the operation of the railway from February 23, 1885, to July 10, 1886, of \$423,142.16. When Clarke and Dillingham took possession of the property of the Railway Company on February 23, 1885, they received in cash \$30,416.34, while they collected for traffic balances

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and other claims \$118,730.08, from sales of old rails on hand February 23, 1885, \$110,275, and from sales of old cars \$6500, making a total of \$265,921.42.

Clarke and Dillingham during the time they were in possession of the property as receivers, and Easton, Rintoul and Dillingham while they were in possession as receivers, expended under the orders of court the following sums outside of operating expenses: \$23,274.20 for liabilities of the Railway Company; \$751,438.15, interest on first mortgage bonds of the Company due January 1 to July 1, 1885; \$245,793.64 for new steel rails; \$125,695.44 for car trust notes; \$265,696.33 for new passenger coaches, baggage, mail and express cars, locomotives, etc.; and \$126,218.62 for right of way, fencing track, real estate, depot, round-house, foundry and pattern-house; in all, \$1,536,116.38, of which \$384,026.20 was expended under the receivership of Clarke and Dillingham. These were the receipts and expenditures up to January 9, 1888, and there was no evidence as to receipts and expenditures after that date.

Easton, Rintoul and Dillingham during their receivership realized out of proceeds of sale or collection of old assets of the defendant company the sum of \$135,889.70.

The receivers in cause 198 received from the receivers in cause 185 the sum of \$138,751.37 in cash.

The receivers in the consolidated cause 198, after taking possession on July 10, 1886, paid liabilities of the receivers, Clarke and Dillingham, taxes, outstanding vouchers, pay rolls, traffic balances, \$221,421.32, and collected from the amount due Clarke and Dillingham as receivers in cause 185 the sum of \$39,016.69.

On the 26th day of November, 1886, the Lackawanna Company filed its petition of intervention in cause 198, praying substantially for the same relief against all the railways, revenues, earnings, moneys and other properties and assets of the defendant company, including those forming the subject-matter of the receivership herein, as was prayed for by its petition of intervention in this cause. Upon that petition the master reported in that cause that under the facts the

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debt for which the company filed its petition was of a character equitably entitling it to be discharged in preference to the mortgage represented in that suit, but which preference should be applicable to so much only of the company's debt as should remain unsatisfied after exhausting the 170 first mortgage five per cent bonds of the Galveston, Harrisburg and San Antonio Railway (Mexican & Pacific extension) of the face value of \$170,000, and which, as heretofore stated, were pledged as security. The Farmers' Loan and Trust Company filed exceptions in that cause to the master's report, but at the date of the master's report in this cause the exceptions had not been brought to a hearing.

The Lackawanna Company on the 30th day of April, 1889, filed suit upon its claims against the Houston and Texas Central Railway Company in the District Court of Dallas County, Texas, a court of competent jurisdiction, and in that suit, after due citation, judgment was rendered against the railway company May 19, 1899, for \$555,914.25 with interest. Upon that judgment execution was issued and was returned August 20, 1899, no property found subject to execution.

Of the interest paid by the receivers on the first mortgage bonds of the defendant railway company, \$79,800 consisted of coupons upon the first mortgage bonds of the company secured by mortgage upon the Waco Division, being the property forming the subject-matter of the litigation herein. Interest was paid upon the coupons representing the same, maturing January 1 and July 1, 1885, to the amount of \$11,571, making a total amount of interest paid to holders of bonds secured by mortgage on the Waco Division of \$91,371, paid May 1, 1887.

During the years 1883 and 1884 the defendant company paid \$2,386,400 interest upon its bonds, which amount, less \$1,043,198.27, borrowed for interest purposes in those years, was presumably (the contrary not appearing) paid from its income or current earnings, and out of said total the sum of \$159,600 was paid as interest upon the first mortgage bonds of the Waco Division, the bonds which are the subject-matter of the bill of complaint in this cause. During 1883 and 1884

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\$2,225,000 approximately were expended from the earnings and general income of the defendant company's property in the payment of interest on bonds and in additional equipments, permanent improvements, etc.

The accounts of the railway company were not kept in such manner as to indicate the exact fund out of which the interest on the first mortgage bonds of the Waco Division was paid, or the exact fund out of which the interest upon the bonds of the other divisions was paid; and no separate account was kept of the earnings of that division as distinguished from the net earnings of the other divisions of the railway company, either prior to or during the receivership thereof, until about April 20, 1889. During the receivership in cause 198, the receivers expended in the payment of interest upon the bonds forming the subject-matter of the bill of foreclosure herein the sum of \$91,371.

By a final decree rendered March 16, 1892, the Circuit Court made in this cause a decree of foreclosure and sale in behalf of the Farmers' Loan and Trust Company. The decree contained these among other provisions:

"And the purchaser or purchasers of said property at said sale shall, as a part of the consideration of the purchase, and in addition to the sum bid, take the property upon the express condition that he or they will pay off, satisfy and discharge any and all claims and interventions now pending and undetermined in this court, accruing prior to the appointment of the receiver herein or during the receivership, which may be allowed and adjudged by this court as prior in right to complainant's mortgage, together with such interest as may be allowed; and also upon the further express conditions that he or they will pay off, satisfy and discharge all debts, claims and demands of whatsoever nature incurred or which may hereafter be incurred by said receiver Charles Dillingham, and which have not been or shall not hereafter be paid by said receiver or other parties in interest herein; and said purchaser or purchasers, their successor or successors, or assigns, shall also have the right to appear and make defence to any claim, debt or demand sought to be enforced against

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said property; and said purchaser or purchasers, their successor or successors, or assigns, shall also have the right to appear and make defence to any claim, debt or demand pending and undetermined at the date of the confirmation of such sale. . . .

"And it is further ordered, adjudged and decreed that it be recited in the deed to be executed and delivered to said purchaser or purchasers, that he or they do take said property, subject to, and that said purchaser or purchasers do assume and agree to pay off any and all debts, claims and demands of whatsoever nature now pending and undetermined, and which may be allowed and adjudged by this court, as prior to any right secured under complainant's mortgage, and subject likewise to all debts, claims and demands of whatsoever nature incurred by Charles Dillingham as receiver in this cause, and which may remain unpaid at the termination of said Dillingham's receivership, provided the same be presented, as hereinbefore provided, within six months after the confirmation of said sale. It is further ordered, adjudged and decreed that the rights of the Lackawanna Coal and Iron Company, the Southern Development Company, the Pacific Improvement Company and the Morgan's Louisiana and Texas Railroad and Steamship Company, intervenors herein, and the rights of all other intervenors herein, be and they are hereby reserved to be hereinafter adjudicated, and are in no manner affected or prejudiced by this decree. It is further ordered that the disposition of any surplus funds arising from the earnings of the road, or otherwise, that may be in the hands of the receiver, is reserved for future determination."

Subsequently, February 26, 1896, a decree was passed in this cause dismissing the intervention herein by the Lackawanna Iron and Coal Company and the Pacific Improvement Company, but without prejudice to the rights of those companies under or by virtue of the intervention in equity cause 198.

This order was affirmed in the Circuit Court of Appeals. 52 U. S. App. 91. The case is now here on certiorari for reëxamination.

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Mr. Maxwell Everts and *Mr. E. B. Kruttschnitt* for the Lackawanna Iron and Coal Company, appellant.

Mr. Herbert B. Turner for the Farmers' Loan and Trust Company, appellee. *Mr. M. F. Mott* was on his brief.

Mr. L. W. Campbell for Moran Bros. and Henry K. McHarg, appellees.

MR. JUSTICE HARLAN, after stating the above facts, delivered the opinion of the court.

In *Southern Railway Co. v. Carnegie Steel Co.*, ante, 257, just decided, we had occasion to consider in the light of our previous decisions the principal questions arising in the present case. We need not repeat here what was said in the opinion in that case as to the general principles applicable in cases involving the respective rights of mortgage creditors and of unsecured creditors in the earnings of an insolvent railroad corporation in the hands of a receiver.

The above statement of the history of this litigation shows that the Houston and Texas Central Railway Company had three contracts with the Lackawanna Company for steel rails; that those contracts were made, respectively, on December 28, 1882, April 26, 1883, and October 30, 1883; and that all the rails delivered under the first contract, and about one half of those delivered under the second contract, were paid for, leaving unpaid for one half of the rails delivered under the second contract and all delivered under the third contract. But the claim for the balance due for rails covered by the contract of April 26, 1883, is abandoned because, as stated by counsel for the Lackawanna Company, it is impossible to state with certainty how many of the rails delivered under that contract were actually used on the Waco Division. We are therefore only concerned in this case with the contract of October 30, 1883, under which rails were delivered.

It also appears that in suit No. 185, brought by the Southern Development Company in February, 1885, receivers were

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appointed of the entire property of the Houston and Texas Central Railway Company, including the Waco Division; that that suit was dismissed in May, 1886, and shortly before that time suits were brought by the trustees of the mortgages on the main line and on the Western Division of that company for the foreclosure of those mortgages, receivers were appointed and the suits were consolidated as Consolidated Case 198; that in the latter cause the entire property was sold September 8, 1888, subject, however, to the first mortgage on the Waco Division; and that the Waco Division was separately sold subject to the first mortgage thereon.

Subsequently, September 6, 1889, the present suit was brought to foreclose the first mortgage on the Waco Division. The Lackawanna Company intervened herein by petition, asking that an account be taken of the amounts due to it, and for a decree "declaring that the sums so due are liens upon the net earnings of said Railway Company, and especially upon those portions of said net earnings which have accrued or may accrue from the railways described in the bill of complaint in this cause, both those accrued prior to said receivership in said cause No. 185, and those accrued and to accrue during the receivership in said cause No. 198, extended to this cause, and upon all of the property of said railway company, superior in rank to the claims of said trustee and of the mortgage bonds and coupons issued under the deed of trust sought to be foreclosed in this cause;" and "that the net earnings of the railway described in the bill of complaint in this cause in the hands of said receiver, accrued or to accrue, be first devoted to the payment of the accounts so decreed, and if they be not sufficient prior to the final decree in this cause to pay said amounts, then that your honors do decree the payment of said amounts out of any proceeds of sale of the property of said Railway Company to be made under said final decree, the amounts so decreed to your petitioner to be paid in preference to any amount due under the mortgage bonds and coupons issued under the deed of trust annexed to the bill of complaint in this cause."

The principal ground upon which the Lackawanna Com-

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pany bases its claim for the relief asked is that when each of the above contracts were made the Waco Division was in such condition that new rails were imperatively required in order that the road might be safely used for the transportation of persons and property. Such, it may be assumed, was the condition of the road when the rails were contracted for and delivered, for it was so found by the master to whom the intervening petition of the Lackawanna Company was referred with direction to take the account prayed for and to report the facts, and to that report no exceptions were filed. But the necessary inference from the report in connection with the averments of the intervening petition is, that the work required to be done in order to put the main road of the Houston and Texas Central Railway Company and its divisions in proper condition was not such as would be done in the ordinary course of the business and operations of a railroad, but was so extensive as to amount to reconstruction, or the construction of new road. That was the view expressed by the Circuit Court of Appeals, and it explains what the master meant by the finding that the debt for which the Lackawanna Company claimed payment could not be classed as a "current debt made in the ordinary course of business." This court has uniformly held that in the distribution of the current earnings of an insolvent railroad company, whose property is being administered by a receiver, mortgage creditors could not be postponed to unsecured creditors, unless the debts due the latter were of the class known as current debts arising in the ordinary course of business and properly chargeable upon current receipts. The decision in each case has been more or less controlled by its special facts. But we are of opinion that such expenditures as those incurred in the making of the contracts with the Lackawanna Company were not such as are made in the ordinary course of the operations of a railroad, and cannot be deemed current debts within the rule that a railroad mortgagee when accepting his security impliedly agrees that the current debts of a railroad company contracted in the ordinary course of its business, in order to keep it a going concern, shall be paid out of current receipts before he has any claim upon

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such income. *Southern Railway Co. v. Carnegie Steel Co.*, ante, 257, and authorities there cited. They are rather to be regarded as extraordinary expenditures, outside of the ordinary course of business and incurred for purposes not of repair but of construction. This court has said that it is the exception, not the rule, that the priority of mortgage liens can be displaced. *Kneeland v. American Loan & Trust Co.*, 136 U. S. 89, 98; *Thomas v. Western Car Co.*, 149 U. S. 95, 111. We have said that priority of unsecured claims is recognized only in a few specified cases in which equity and good conscience require that the vested liens of mortgage creditors shall be postponed in the application of current earnings to current debts. Sound principle forbids that a court of equity should imply an agreement upon the part of mortgage creditors to subordinate their claims to such debts as those due to the Lackawanna Company. To so hold would place their rights at the mercy of the railroad company having charge of the property upon which their recorded liens rest. Besides, the rails in question were delivered long before the railroad company had made any default in the payment of interest; about sixteen months before the company's property was put into the hands of a receiver, and about five and a half years before the appointment of a receiver in this cause. Then there is the circumstance that the Lackawanna Company, during the negotiations resulting in the execution of renewal notes under the second contract for rails, demanded and received collateral security to a large amount from the railroad company—a circumstance tending to show that it did not regard itself as entitled to an equitable claim upon net earnings in preference to mortgage creditors, but relied upon the general credit of the railroad company. However meritorious the claim of the Lackawanna Company may be as between it and the railroad company, we cannot by reason of anything appearing in the record impair or displace the liens of mortgage creditors for its benefit. Under all the circumstances, including the amount of the debt and the long period of credit, the claims in question must be regarded as general unsecured debts, not contracted in the ordinary course of business, and

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with the expectation of the parties that they were to be met out of current receipts in preference to claims of mortgage creditors. It is not therefore entitled to the priority claimed. The view taken of the case by the Circuit Court of Appeals is indicated by Judge Parlange, whose opinion, on behalf of that court, thus concludes: "The unusually large purchase of rails, the time within which they were to be delivered, the condition of the road, the contracts providing for notes at six months renewable for a like term at the maker's option, the hypothecation of securities for the payment of the claim, the knowledge which the intervenor had of the mortgage, the fact that the contracts contained no promise to pay out of any particular fund, the time which elapsed between the date of the contracts and the appointment of a receiver in cause No. 185 — are circumstances which, taken together, cannot fail to convince us that the intervenor relied upon the general credit of the railway company."

The decree of the Circuit Court of Appeals is therefore

Affirmed.